DOCKET

SUPREME COURT
OF THE UNITED STATES

No. 09-1298
Vide 09-1302
Title: General Dynamics Corporation, Petitioner
v.
United States
Docketed: April 27, 2010
Linked with 09A705
Lower Ct: United States Court of Appeals for the Federal Circuit
Case Nos.: (2007-5111, 2007-5131)
Decision Date: June 2, 2009
Rehearing Denied: November 24, 2009
Questions Presented

~~Date~~~	~~~~~~~Proceedings and Orders~~~~~~~~~~~~~~~~~~~~~
Jan 26 2010	Application (09A705) to extend the time to file a petition for a writ of certiorari from February 22, 2010 to March 24, 2010, submitted to The Chief Justice.
Jan 28 2010	Application (09A705) granted by The Chief Justice extending the time to file until March 24, 2010.
Mar 10 2010	Application (09A705) to extend further the time from March 24, 2010 to April 23, 2010, submitted to The Chief Justice.
Mar 11 2010	Application (09A705) granted by The Chief Justice extending the time to file until April 23, 2010.
Apr 23 2010	Petition for a writ of certiorari filed. (Response due May 27, 2010)
Apr 23 2010	Appendix of General Dynamics Corporation filed.
May 18 2010	Order extending time to file response to petition to and including June 28, 2010.
May 27 2010	Brief amicus curiae of National Defense Industrial Association filed. VIDED.
May 27 2010	Brief amicus curiae of Chamber of Commerce of the United States of America filed. VIDED.
Jun 18 2010	Order further extending time to file response to petition to and including July 28, 2010.
Jul 7 2010	Order further extending time to file response to petition to and including August 20, 2010.
Aug 20 2010	Brief of respondent United States in opposition filed. VIDED.
Aug 31 2010	Reply of petitioner General Dynamics Corporation filed.
Sep 1 2010	DISTRIBUTED for Conference of September 27, 2010.
Sep 28 2010	Petition GRANTED limited to Question 1 presented by the petition. The petition for a writ of certiorari in No. 09-1302 is granted limited to Question 2 presented by the petition. The cases are consolidated and a total of one hour is allotted for oral argument.
Oct 5 2010	Consent to the filing of amicus curiae briefs in support of either party or neither party received from counsel for petitioner General Dynamics Corp. VIDED.
Oct 11 2010	Consent to the filing of amicus briefs, in support of either party or of neither party, received from counsel for petitioner Boeing Company. VIDED.
Oct 12 2010	Consent to the filing of amicus briefs, in support of either party or of neither party, received from counsel for the respondent. VIDED.
Nov 8 2010	SET FOR ARGUMENT ON Tuesday, January 18, 2011.
Nov 12 2010	Brief of petitioner General Dynamics Corporation filed. VIDED.
Nov 12 2010	Joint appendix filed (3 volumes). Statement of costs filed. VIDED.
Nov 12 2010	Brief of petitioner The Boeing Company filed. VIDED.
Nov 17 2010	Brief amici curiae of Al-Haramain Islamic Foundation, Inc., et al. filed. VIDED.
Nov 19 2010	CIRCULATED.

Nov 19 2010	Brief amicus curiae of Constitution Project filed. VIDED. (Distributed)
Nov 19 2010	Brief amici curiae of Chamber of Commerce of the United States of America filed. VIDED. (Distributed)
Nov 19 2010	Brief amici curiae of National Defense Industrial Association filed. VIDED. (Distributed)
Nov 23 2010	Letter, dated November 23, 2010, notifying the Court that Carter Phillips has been engaged to represent petitioners in oral argument received.
Dec 13 2010	Brief of respondent United States filed. VIDED. (Distributed)
Dec 13 2010	Record received from U.S.C.A. for Federal Circuit. (1 box)
Jan 4 2011	Reply of petitioner General Dynamics Corporation filed. VIDED. (Distributed)
Jan 4 2011	Reply of petitioner The Boeing Company filed. VIDED. (Distributed)
Jan 18 2011	Argued. For petitioners: Carter G. Phillips, Washington, D.C. For respondent: Neal Kumar Katyal, Acting Solicitor General, Department of Justice, Washington, D.C.

PETITION FOR WRIT OF CERTIORARI

Supreme Court, U.S.
FILED

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OFFICE OF THE CLERK

No.

IN THE
Supreme Court of the United States

GENERAL DYNAMICS CORPORATION,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

On Petition For A Writ Of Certiorari To The
United States Court Of Appeals
For The Federal Circuit

PETITION FOR WRIT OF CERTIORARI

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April 23, 2010

QUESTIONS PRESENTED

1. Whether the government can maintain its claim against a party when it invokes the state-secrets privilege to completely deny that party a defense to the claim.

2. Whether, contrary to nearly a century of government contracts law, a court can uphold a default termination on factual grounds never relied on by the contracting officer, and can dispense with the requirement that the contracting officer exercise discretion when terminating for default.

3. Whether one panel of a court of appeals can use the law-of-the-case doctrine to overrule another panel's prior decision in the same case as clearly erroneous or manifestly unjust and thereby circumvent the law-of-the-circuit doctrine, which permits only the *en banc* court to overrule a precedential panel decision.

LIST OF PARTIES

Pursuant to Rule 14.1(b) and Rule 29.6, the following list identifies all the parties to the proceeding before the United States Court of Appeals for the Federal Circuit:

General Dynamics Corporation, appellant below, has no parent corporation. No publicly held company owns ten percent or more of the stock of General Dynamics Corporation.

McDonnell Douglas Corporation, appellant below, was a wholly owned subsidiary of The Boeing Company prior to January 1, 2010. On January 1, 2010, McDonnell Douglas Corporation was merged into The Boeing Company, which is now the corporate successor of McDonnell Douglas Corporation. The following publicly held companies own ten percent or more of the outstanding stock of The Boeing Company: State Street Corporation and its subsidiary State Street Bank and Trust Company as the trustee of The Boeing Company Employee Savings Plan Master Trust; Evercore Trust Company, N.A. as the investment manager of The Boeing Company Employee Savings Plan Master Trust.

The United States.

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OPINIONS BELOW

The opinions of the Federal Circuit (Pet. App. 1a-34a, 178a-211a, 250a-279a) are reported at 182 F.3d 1319, 323 F.3d 1006, and 567 F.3d 1340. The order of the Federal Circuit denying the petition for panel rehearing or rehearing *en banc* (Pet. App. 444a-445a) is unreported. The pertinent opinions of the Court of Federal Claims (Pet. App. 35a-177a, 212a-249a, 280a-443a) are reported at 29 Fed. Cl. 791, 35 Fed. Cl. 358, 37 Fed. Cl. 270, 40 Fed. Cl. 529, 50 Fed. Cl. 311, and 76 Fed. Cl. 385.

JURISDICTION

The Court of Appeals for the Federal Circuit issued its decision on June 2, 2009. On November 24, 2009, the Federal Circuit denied petitioner's timely filed petition for rehearing or rehearing *en banc*. Chief Justice Roberts extended the time for filing a petition for certiorari to April 23, 2010. The jurisdiction of this Court is properly invoked pursuant to 28 U.S.C. § 1254(1).

STATUTES AND REGULATORY PROVISIONS INVOLVED

This case involves the following statutes and regulatory provisions, which are set forth in full in the Appendix to the Petition (Pet. App. 446a-472a): 41 U.S.C. § 605; 48 C.F.R. § 49.402-3; *id.* § 52.249-2; *id.* § 52.249-9.

STATEMENT OF THE CASE

A. Factual Background

General Dynamics Corporation and McDonnell Douglas Corporation (together, the "contractors") were awarded a multi-billion-dollar contract by the Navy to jointly design, develop, and build a state-of-the-art weapon system called the "A-12 Avenger." The A-12 was to be a stealth aircraft that would expand upon technology already in use in other government programs. The ultimate aim of the contract was a fully validated aircraft design; thus, the contract called for a series of increasingly sophisticated aircraft to be built and extensively tested.

The contractors were promised that the government would share its exclusive knowledge regarding stealth technology, and that this would be the foundation for the stealth capabilities in the A-12. Pet. App. 353a-355a & n.6. However, in an about-face, the government ultimately refused to give the relevant information to the contractors. *Id.* 52a & n.9.

Without the promised technology, it became apparent that some of the "A-12 performance specifications were impossible to accomplish within the time and cost projections contemplated by the parties." *Id.* 355a. After extraordinary efforts, the contractors informed the Navy that they would not be able to meet the original weight specification or the original contract schedule, which included a number of interim milestones. *Id.* 385a-387a. The Navy responded by waiving both requirements. It

relaxed the weight specification, accepted the contractors' aircraft design, *id.* 156a-157a, 388a-389a, and extended the schedule for delivery of the first eight aircraft under contract, *id.* 71a. The Navy left the schedule for delivery of the remaining six aircraft undefined, however, and never set a new completion date for the entire contract effort, which included years of ground and flight testing. *Id.* 71a-72a.

In addition, because the contractors had been forced to reinvent the wheel when it came to stealth technology, the costs of performing the contract had far exceeded the amounts obligated by the government. Thus, the contractors also requested financial relief. *Id.* 95a-96a. The government denied that request. Nevertheless, the contractors stated that they remained committed to the A-12 program. *Id.* 148a-149a & n.82.

Despite the Navy's and the contractors' desire to continue the A-12 development effort, political support at higher levels in the Pentagon was waning. With the Cold War over, the Pentagon reviewed its spending priorities, and the A-12 program fell victim to that review. *Id.* 389a-391a. Thus, although the Navy's contracting officer strongly supported the A-12 program and did not believe the contractors were unwilling or unable to complete the contract, and although the contractors had not missed *any* of the interim deadlines set forth in the Navy's revised schedule, Secretary of Defense Cheney ordered the termination of the program. *Id.* 395a-398a. That order reflected amorphous "concerns" about contract cost and schedule, but came without any

"consideration of the contract's circumstances." *Id.* 387a, 391a-397a, 414a.

The Navy was scheduled to obligate an additional $553 million in funds to the contract the very next day. *Id.* 399a. To avoid this obligation, the contracting officer precipitously terminated the contract for default. A default termination must be based on some contractor wrongdoing, and is a "drastic sanction," *J.D. Hedin Constr. Co. v. United States*, 408 F.2d 424, 431 (Ct. Cl. 1969), pursuant to which the contractor is denied any payment for costs that have not yet been reimbursed and may be required to return payments it has received for work that the government has not yet officially "accepted." 48 C.F.R. § 52.249-9. A default termination also can result in the contractor being debarred from public contracting, *id.* § 9.406-2(b)(1), or prejudiced in the award of new contracts, *id.* § 15.304(c)(3). The other way for the government to terminate a contract is a "termination for convenience," which allows the government to act without fear of incurring any damages for breach. The government must reimburse the contractor for certain costs reasonably incurred, but otherwise is entitled simply to walk away. *Id.* § 52.249-2.

To justify terminating the A-12 contract for default rather than for convenience, the contracting officer and Navy counsel were forced to cobble together a termination memorandum in very short order. Pet. App. 399a-403a. Because the termination came early in the life of this multi-year contract, the stated basis for the termination was a projected failure to "[p]rosecute the work" so as to

make adequate progress (as opposed to a failure to meet a deadline that had already passed), 48 C.F.R. § 52.249-9(a)(1)(ii) – but the contracting officer did not perform any analysis at all of the contractors' progress or performance. Pet. App. 410a-411a. Instead, he simply "cribbed" a prior termination memorandum from a completely unrelated program. *Id.* 411a. Thus, the "termination memorandum for the A-12 reflect[ed] an analysis conducted for the P-7 program, not the merits [of the contractors'] performance on the A-12." *Id.* 100a.

As a result, the memo contained a number of glaring mistakes and omissions. Most significantly, the contracting officer terminated the contractors for failure to make progress toward the completion of the contract, yet left blank the completion date. *Id.* 142a. That was not surprising, since at the time there was no completion date for the contract. *Id.* 14a.

Following the default termination, the Navy sent the contractors a letter demanding the return of approximately $1.35 billion in progress payments, plus interest.

B. Procedural History

Pursuant to the Contract Disputes Act, the contractors challenged the default termination in the Court of Federal Claims. In this action, the government bore the burden of proof to justify its decision to terminate for default, which constitutes a government claim. The *only* consequence to the government of a failure to meet this burden is a

conversion of the default termination to a termination for convenience.

1. After a trial, the Court of Federal Claims first ruled for the contractors. It found in no uncertain terms that "the A-12 contract was not terminated because of contractor default. The contract was terminated because the Office of the Secretary of Defense withdrew support and funding from the A-12." *Id.* 383a.

In support of this conclusion, the trial court found that the government's contracting officer "did not review any A-12 contract documents in preparation for the termination. He did not consult with technical personnel.... He did not review documents related to schedule or specifications." *Id.* 401a-402a. The court concluded that "[t]he entire termination procedure was *pro forma* at best" and that "the reasons [for termination] were not contractor performance or default." *Id.* 412a-413a. The court thus converted the default to a termination for convenience. It found that the contractors were entitled to $1.2 billion in unreimbursed costs reasonably incurred in their performance, plus interest. *Id.* 341a-342a.

The government appealed to the Federal Circuit, which reversed and remanded. The court of appeals held that a potentially valid default termination requires only some "nexus" between the government's termination for default and the contractor's performance, *id.* 269a, and concluded that "because the termination for default was predicated on contract-related issues, it was within

the discretion of the government," *id.* 251a.[1] The Federal Circuit left it for the trial court to decide, however, whether the default termination was actually justified in light of the contractors' performance.

2. After another trial, the court upheld the termination for default on the sole basis that the contractors were not projected to meet the deadline for one early milestone in the multi-year, multi-billion-dollar contract. That milestone was the date for "first flight" of the first A-12 test aircraft. *Id.* 212a, 248a-249a. The court did not look to any date beyond that milestone, or assess how long it would have taken the contractors to perform the entirety of the contract effort.

Separately, the trial court held that it would not entertain the contractors' defense that their delay was entirely excusable due to the government's failure to share its superior knowledge regarding stealth technology. *Id.* 246a. The government had unilaterally invoked the state-secrets privilege – which applies if "there is a reasonable danger" of exposure of "military matters which, in the interest of national security, should not be divulged," *United States v. Reynolds*, 345 U.S. 1, 10 (1953) – to bar the litigation of issues relating to that technology. Once the government asserted that privilege, the trial court ruled that the contractors' "superior knowledge

[1] In the wake of this decision, General Dynamics filed a petition for certiorari. The government argued that the petition was premature because the decision was interlocutory, and this Court denied the petition. *See McDonnell Douglas Corp. v. United States*, 120 S. Ct. 1831 (2000).

defense could not be tried because the resulting threat to national security would not permit it." Pet. App. 243a-244a.

The contractors appealed, and the Federal Circuit affirmed in part and reversed in part. The Federal Circuit affirmed the trial court's ruling regarding the superior-knowledge defense. It found that the requirements for invoking the state-secrets privilege were satisfied, and rejected the contractors' argument that the government could not pursue a default claim while stripping the contractors of a defense to that claim. *Id.* 202a-210a.

As to the default termination, however, the Circuit reversed and remanded. The court explained that the contractors could not properly be defaulted for a projected failure to meet a single interim milestone. Rather, the court held, the governing standard was set forth in *Lisbon Contractors, Inc. v. United States*, 828 F.2d 759 (Fed. Cir. 1987): the trial court had to determine "the actual performance that the contract requires and the amount of time remaining for that performance," and then decide whether there was a "reasonable belief on the part of the contracting officer that there was no reasonable likelihood that the contractor could perform the entire contract effort within the time remaining for performance." Pet. App. 191a, 195a. As the court of appeals stated, "[u]nless the contracting officer had determined the entire effort required under the contract and the time left to complete the contract, it would be difficult, if not impossible, for him to resolve" this question. *Id.* 195a.

3. On remand, the trial court recognized that the contracting officer had never made the determination required by the Circuit, and could not have done so. As the court stated, the "contracting officer did not know [at the time of termination] when contract completion might occur," *id.* 39a, and "did not conduct a *Lisbon* analysis prior to termination," *id.* 176a n.92. Thus, "[t]he A-12 termination memorandum did not reflect any contracting officer analysis of the time when the A-12 contractors were likely to complete the remaining contract effort." *Id.* 101a n.42. Nor could it have done so, since at that time there was no date in place for completion of the entire effort. *Id.* 73a.

The trial court acknowledged that the contractors would therefore prevail if "the clauses 'entire contract effort' and 'contract completion date'" in the Circuit's mandate "mean exactly what they appear to mean." *Id.* 176a n.92; *see also id.* 39a ("[I]f the date we must look to in measuring the contractors' progress can occur no earlier than after completion of plaintiffs' contract requirements, we would vacate the termination for default."). But the trial court refused to undertake the analysis mandated by the Federal Circuit, and instead simply found that if the "Government can point to reasons in retrospect why plaintiffs were not making the progress that some officials hoped and perhaps expected[,] [s]o long as those reasons form a rational basis for a reviewing court to uphold defendant's decision to terminate, the court must do so." *Id.* 176a. The court upheld the termination for default on that basis.

The contractors again appealed, and this time the Federal Circuit affirmed. The Circuit agreed with the contractors that at the time of termination there was no contract completion date in place, and thus no way to assess whether the contractors were making adequate progress toward completion of the whole contract. *Id.* 13a-14a. But the court of appeals changed the legal standard, concocting what it described as an "ad hoc, factual" test to measure the contractors' progress. *Id.* 20a-21a. The court then held that the government had carried its burden because the "contractors' performance history," including their failure to meet early deadlines under the *original* schedule that the government had waived and reset, "shows that the contracting officer was reasonably justified in feeling insecure about the contractors' rate of progress," *id.* 27a. Despite acknowledging the absence of a completion date, the court repeatedly referred to the concept of "timely completion" when explaining how this "ad hoc" test was to be applied. *Id.* 15a, 21a-22a, 28a.

The panel expressly acknowledged that the new test differed from the one that the prior panel had mandated. *Id.* 27a n.4. But the court stated that it "believe[d] that this is warranted as under the law of the case doctrine, 'it is not improper for a court to depart from a prior holding if convinced that it is clearly erroneous and would work a manifest injustice.'" *Id.* The court provided no explanation of why the prior opinion had been clearly erroneous, or why converting the default termination into a

termination for convenience would work a manifest injustice.

The court also gave the contractors no opportunity to show that they could prevail under the new standard. Instead, the Federal Circuit affirmed on factual grounds different from (and contrary to) those relied upon by either the contracting officer or the trial court, stating only that "the facts in the record are sufficient for the court, in a de novo review, to sustain the default termination." *Id.* 32a.

On December 29, 2009, the government sent the contractors a letter demanding payment of $1,352,459,644 plus statutory interest from 1991, for a total (as of the filing of this petition) of nearly $2.9 billion.

REASONS FOR GRANTING THE PETITION

This case comes to this Court after nearly twenty years of litigation over whether the government was justified in imposing the drastic sanction of a default termination when it chose to cancel the A-12 program. In the first phase of the case, when memories were fresh, the trial court heard the evidence and concluded that the claimed reasons for the default termination, pursuant to which the government seeks billions of dollars from the contractors, were entirely pretextual. That finding has never been disturbed. But the Federal Circuit has since issued three different decisions, each struggling to find a legal basis for upholding a politically motivated default. In so doing, the court of appeals has generated several rulings that raise

issues of enormous importance warranting this Court's review.

First, the Federal Circuit grossly misapplied the state-secrets doctrine. The court held that the government could pursue its claim for default termination against the contractors while at the same time using the state-secrets privilege to entirely deprive them of one of their principal defenses: that they were unfairly disadvantaged by the government's refusal to share its stealth technology. In so holding, the court disregarded the clear teachings of this Court's state-secrets jurisprudence, basic principles of due process, and numerous contrary rulings from other circuits.

Second, ignoring applicable regulations and many decades of precedent, the court of appeals held that the default could be upheld even if the contracting officer *never actually weighed the issue* and exercised discretion, and even if the factual basis *was never even articulated* at the time of termination. The court thus adopted an approach that would never be tolerated for a moment in any other area of administrative law. Moreover, the court of appeals applied an ad hoc balancing test that makes it nearly impossible for contractors to combat unjustified default terminations. These troubling rulings came from the court charged with handling almost all litigation over government contracts, and thus will have national impact. For that reason, and because the rulings may ultimately force potential government contractors to refuse to undertake research-and-development contracts like the A-12

contract, the rulings strongly merit this Court's attention.

Finally, in reversing course to invent its new ad hoc balancing test, the Federal Circuit panel did not even bother to call for *en banc* review of the prior panel decision in this case setting a dramatically different legal standard. It invoked the law-of-the-case doctrine, holding that a panel has the power to overrule a prior panel decision by labeling it clearly erroneous or manifestly unjust. That approach has been flatly rejected by several other circuits, which have recognized that law-of-the-case doctrine does not provide an exception to the rule that only the *en banc* court can overrule a prior panel decision. The Federal Circuit's approach is also inconsistent with the sound administration of a court composed of multiple judges who hear cases in panels. In this case, it serves to dramatize the lengths to which the court was willing to go to uphold a default that was long ago found pretextual – and that now forms the basis of a government demand for a multi-billion-dollar forfeiture from two of the Nation's most important defense contractors.

I. The Federal Circuit's Decision Conflicts With This Court's Precedent and Decisions in Other Circuits on the Consequences of Successful Assertion of the State-Secrets Privilege.

The contractors had what both courts below recognized as a strong defense to the government's claim that the A-12 contract was properly terminated for default: that the government had "superior knowledge" of the stealth technology required to

develop the A-12 but refused to share it with the contractors, leading to the very delay that was the basis for the alleged failure to make adequate progress. As the trial court explained, the contractors "made a persuasive showing that they could prove" the superior-knowledge defense without resort to any secret information. Pet. App. 245a; *see also id.* 270a-272a; *Helene Curtis Indus., Inc. v. United States*, 312 F.2d 774, 777-79 (Ct. Cl. 1963). Nevertheless, based on the government's assertion that it could not counter the defense without resort to state secrets, the trial court barred the contractors from pressing their argument, and the Federal Circuit affirmed, ultimately upholding the government's claim. Pet. App. 245a-246a, 353a-381a, 202a-210a.

Petitioner is in no position to challenge the government's assertion of the state-secrets privilege in the first instance, or even the lower courts' determination that the superior-knowledge issue could not be litigated without risking disclosure of secret information. At issue here, rather, are the *consequences* of the government's assertion of the privilege.

In allowing this case to proceed, the Federal Circuit upheld a result that is, under this Court's precedents, "unconscionable." *Reynolds*, 345 U.S. at 12; *see also Roviaro v. United States*, 353 U.S. 53, 60-61 (1957); *Jencks v. United States*, 353 U.S. 657, 671 (1957). As a general matter, it is well established that a court should not exercise its power to uphold a claim where the state-secrets privilege deprives a party of a potentially valid defense to that

claim. Moreover, as this Court has explained, it is particularly pernicious to permit the government to prosecute its *own* claim while using the state-secrets privilege to ensure that the claim is not defeated, since "the Government which prosecutes an accused also has the duty to see that justice is done." *Reynolds*, 345 U.S. at 12. The Federal Circuit's ruling cannot be reconciled with these elemental principles of justice, and conflicts with the decisions of this Court and of other circuits.

1. This Court's decision in *United States v. Reynolds*, 345 U.S. 1 (1953), established the specific principle that the government cannot use the state-secrets privilege to eliminate an obstacle to its own claim for relief. In *Reynolds*, the Court stated that it would be "unconscionable" for the government to "prosecute[ ] an accused" while at the same time using the privilege to "deprive the accused" of a defense. *Id.* at 12. The Court also explained that this principle has no application where "the Government is not the moving party." *Id.* But where the government *is* the moving party, a court will not permit the government to ensure its own victory – and its opponent's punishment – through the government's exercise of its virtually unreviewable discretion to identify and protect state secrets. Thus, the government must choose between invoking the privilege and pursuing its claim.[2] *See id.*; *see also*

[2] The government is not put to such a choice where, as in *Reynolds* itself, the assertion of the privilege deprives a *claimant* of evidence to aid in its affirmative case. In such circumstances, a court has no obvious way to remedy any

Jencks, 353 U.S. at 670 (even though "the protection of vital national interests may militate against public disclosure of documents in the Government's possession," the government may not pursue a prosecution if it withholds such documents); *Roviaro*, 353 U.S. at 60-61 (addressing informer's privilege and holding that the government cannot continue to prosecute its claim while withholding information that is "relevant and helpful to the defense" or "essential to a fair determination of a cause").

This case exhibited exactly the kind of government conduct that *Reynolds* condemned. Here, the government is indeed the "moving party," 345 U.S. at 12 – and, contrary to the Federal Circuit's belief, Pet. App. 208a-209a, that is indisputably so even though the contractors are nominally the plaintiffs. The claim that the contractors defaulted on the A-12 contract is without question a "government claim." *Malone v. United States*, 849 F.2d 1441, 1443 (Fed. Cir. 1988). Once the contractors initiated suit, the government bore the burden of proof to establish the existence of default and to justify a default termination. *See, e.g.*, Pet. App. 196a-197a; *Lisbon*, 828 F.2d at 763-64. And the government seeks to recover an enormous sum from the contractors as a result of the court's ruling upholding the default termination. *See supra* p. 11. Thus, while the contractors appear as "plaintiffs" in the caption, that is simply a result of the way the government itself has chosen to structure the proceedings, *see, e.g.*, *Seaboard*

resulting unfairness, and the claimant must proceed as best it can with the evidence that remains.

Lumber Co. v. United States, 903 F.2d 1560, 1562-63 & n.4 (Fed. Cir. 1990), and the contractors' case here is in every meaningful sense an effort to oppose a claim by the government.

By invoking the state-secrets privilege, the government has not simply taken some evidence out of this case; rather, it has entirely prevented the contractors from raising a critical defense. *See, e.g.*, 2009 Oral Arg. 1:12:44 - 1:13:02 (Chief Judge Michel: "[I]t looks to me as if had the Air Force [stealth] technology been handed over at the start of this contract to the two companies, ... they would have met the dates, and the Navy would have got the plane it needed and wanted"), *available at* http://oralarguments.cafc.uscourts.gov/mp3/2007-5111Pt1.mp3. The Federal Circuit nevertheless refused to bar the government from continuing to pursue the matter. In so ruling, the court permitted the very unfairness that the *Reynolds* Court prohibited. *See* 345 U.S. at 12; *see also Roviaro*, 353 U.S. at 60-61 (discussing "fundamental requirements of fairness").

That violation was particularly "unconscionable" because default termination – although technically a civil sanction – is a "species of forfeiture" with consequences sufficiently grave that it is not far removed from criminal prosecution. *DeVito v. United States*, 413 F.2d 1147, 1153 (Ct. Cl. 1969). Default termination jeopardizes a contractor's ability to obtain future government contracts. *See, e.g.*, *Bannum, Inc. v. United States*, 91 Fed. Cl. 160, 171 (2009). It also results in the contractor's forfeiture of amounts that it would otherwise be entitled to

receive for work underway. In this case, the sanction against the contractors could total billions of dollars, and the contractors will also be deprived of billions of dollars that they would have received had the government terminated for convenience. These realities confirm that default termination is a "drastic" and "severe" penalty, *J.D. Hedin*, 408 F.2d at 431; *see also Schlesinger v. United States*, 390 F.2d 702, 709 (Ct. Cl. 1968) – one that puts the contractor in the position of an "accused," *Reynolds*, 345 U.S. at 12.

Accordingly, this case falls squarely within the rule that a court will not put its stamp of approval on a claim where the state-secrets privilege vitiates a defense to that claim – and, more specifically, that "it is unconscionable to allow [the government] to undertake prosecution and then invoke its governmental privileges to deprive the accused of anything which might be material to his defense." *Id.* The Federal Circuit's decision is thus not only deeply unfair, but wholly inconsistent with *Reynolds* and with other precedent of this Court, including the many decisions establishing that in both civil and criminal cases "[d]ue process requires that there be an opportunity to present every available defense." *Lindsey v. Normet*, 405 U.S. 56, 66 (1972) (quoting *American Surety Co. v. Baldwin*, 287 U.S. 156, 168 (1932)); *see also Roviaro*, 353 U.S. at 60-61; *Jencks*, 353 U.S. at 671.[3]

[3] *See also, e.g., United States v. Andolschek*, 142 F.2d 503, 506 (2d Cir. 1944) (Hand, J.), *cited in Roviaro*, 353 U.S. at 61, *Jencks*, 353 U.S. at 671, and *Reynolds*, 345 U.S. at 12 n.27.

2. The Federal Circuit's decision also directly conflicts with decisions of the Fourth, Sixth, and D.C. Circuits, which have recognized the overarching principle that a claim cannot proceed where the state-secrets privilege deprives a party of a potentially valid defense. *See Tenenbaum v. Simonini*, 372 F.3d 776, 777 (6th Cir. 2004); *Molerio v. FBI*, 749 F.2d 815, 825 (D.C. Cir. 1984) (Scalia, J.); *El-Masri v. United States*, 479 F.3d 296, 309-10 (4th Cir. 2007); *see also Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 547 (2d Cir. 1991) (acknowledging this rule without applying it); *In re United States*, 872 F.2d 472, 476-77 (D.C. Cir. 1989) (same); *Kasza v. Browner*, 133 F.3d 1159, 1166 (9th Cir. 1998) (same).[4]

For instance, in *Tenenbaum*, the Sixth Circuit affirmed the dismissal of a suit against the United States and various federal employees alleging a biased criminal investigation because "the state secrets doctrine ... deprives [d]efendants of a valid defense to the [plaintiffs'] claims." 372 F.3d at 777. The court concluded that where the defendants could not "defend their conduct ... without revealing the privileged information," the suit could not go forward. *Id.*

Likewise, in *Moliero*, the D.C. Circuit held that a plaintiff alleging that the FBI violated his First Amendment rights in failing to hire him could not

[4] Consistent with this principle, other circuits have also held that the government may not use the state-secrets privilege to deprive a criminal defendant of a defense. *See, e.g., United States v. Aref*, 533 F.3d 72, 79 (2d Cir. 2008); *United States v. Klimavicius-Viloria*, 144 F.3d 1249, 1261 (9th Cir. 1998).

pursue his claim where the invocation of the state-secrets privilege barred the government from asserting a defense. 749 F.2d at 825 (Scalia, J.). The court concluded that in the absence of the secret information that would have allowed the government to defeat the claim, the case simply could not proceed: although there may have been "enough circumstantial evidence to permit a jury" to rule in favor of the claimant, that result would have been a "mockery of justice." *Id.*; *see also In re Sealed Case*, 494 F.3d 139, 148-51 (D.C. Cir. 2007).

Similarly, in *El-Masri*, the Fourth Circuit dismissed a complaint against United States officials and various corporate defendants seeking damages for alleged violations of the Due Process Clause and the Alien Tort Statute. The court held that any of the "main avenues of defense available in this matter" would impermissibly require disclosure of state secrets. 479 F.3d at 309. The court concluded that the alleged wrongdoers therefore "could not properly defend themselves," and it ended the case against them. *Id.*

To be sure, some of the claims dismissed in these cases were filed against the government, and the government therefore deprived *itself* of a defense when it chose to invoke the state-secrets privilege. But the cases do not suggest that the outcome should be different when the government is asserting a claim and a private party is defending against it. Indeed, given that the state-secrets privilege can be asserted solely by the government, *see Reynolds*, 345 U.S. at 7, the unfairness of allowing a claim to proceed where the privilege hampers a defense is

only heightened when the government is the party seeking to enforce some penalty. Not surprisingly, then, courts have often recited the applicable rule in a manner that does not distinguish between claims against the government and claims by the government. *See Zuckerbraun*, 935 F.2d at 547; *Kasza*, 133 F.3d at 1166.

3. Even apart from the serious conflicts described above, the state-secrets issue presented here is one of exceptional importance. The result permitted by the Federal Circuit is that two of the Nation's most important defense contractors are called on to forfeit billions of dollars, despite having a valid defense to the government's charges of default. Such a "mockery of justice" should not be allowed to stand. *Moliero*, 749 F.2d at 825.

In addition, the Federal Circuit has established a rule that will be binding in nearly every government contracts case, since (with very few exceptions) no other circuit has jurisdiction over such matters. *See* 28 U.S.C. § 1295(a)(3), (10); *id.* § 1491(a)(1)-(2); *id.* § 1346(a)(2). That rule creates a dangerous precedent in a field where contractors frequently work with and develop classified technology. Under the Federal Circuit's decision, the government may affirmatively proceed against a contractor, obtaining a large financial recovery, even while invoking the state-secrets privilege to eliminate the contractor's defense. The temptations of that option for the government, and the resulting disincentives for private contractors to enter into certain contracts that are necessary to the country's welfare, are intolerable. *See United States v. Winstar Corp.*, 518

U.S. 839, 913 (1996) (Breyer, J., concurring) (government may be unable "to obtain needed goods and services" if parties are "unwilling to undertake the risk of government contracting").

The nature of the state-secrets privilege increases the potential for abuse. The basis for the government's invocation of the privilege is often immune from even *in camera* review, *see, e.g.*, *Reynolds*, 345 U.S. at 10, and history shows that the government has sometimes asserted the privilege without justification, as in *Reynolds* itself. *See, e.g.*, Meredith Fuchs, *Judging Secrets: The Role Courts Should Play in Preventing Unnecessary Secrecy*, 58 Admin. L. Rev. 131, 168 (2006).[5]

Cases do exist in which vital state secrets necessitate keeping certain information confidential. But the costs of that confidentiality should not be borne by individual contractors subject to a massive forfeiture. This Court should confirm that when the government, acting as the "moving party," asserts the state-secrets privilege to bar its opponent's defense, it can protect its secrets only at the expense of its claim.

[5] The government's recent guidelines for invoking the privilege do not erase the potential for abuse, since the government retains virtually unreviewable control over the matter. *See* Office of the Attorney General, *Policies and Procedures Governing Invocation of the State Secrets Privilege* (Sept. 23, 2009), *available at* http://www.justice.gov/opa/documents/state-secret-privileges.pdf.

II. The Federal Circuit's Unprecedented Decision to Permit Default Termination Without a Contracting Officer Assessment of Performance, and on a Rationale Not Articulated at the Time of Termination, Will Have Broad Application and Is of Crucial Importance.

The Federal Circuit held that the government can terminate a contract for default without the contracting officer's performing any evaluation of a contractor's actual performance. Moreover, it held that a court adjudicating the propriety of the default termination need not confine its review to the government's contemporaneous justification for the default termination, but can instead uphold the termination on any ground at all, even if it was never considered or articulated when terminating the contract. These rulings upset nearly a century of settled government contracts law, conflict with basic principles of judicial review of administrative action, and result in a regime in which the government has essentially unbridled authority to subject contractors to a drastic penalty. The rulings not only changed the outcome here, but also put at risk existing and future government contracts, including those for critical military projects. Because the Federal Circuit has exclusive jurisdiction under the Contract Disputes Act, *see* 28 U.S.C. § 1346; *id.* § 1491, there can be no conflict with another circuit on these issues, but the issues are of serious national importance, and this Court's review is urgently necessary. *See, e.g., eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388, 391 (2006) (granting certiorari to "determine the appropriateness" of "general rule"

applied by Federal Circuit in area of its exclusive jurisdiction).

1. The Federal Circuit has stripped away vital protections for contractors that are mandated by statute and regulation and are embodied in precedent of the Circuit and its predecessor court stretching back almost a century. Under the Contract Disputes Act, "[a]ll claims by the government against a contractor relating to a contract shall be the subject of a decision by the contracting officer." 41 U.S.C. § 605(a). Further, "[t]he contracting officer shall issue his decisions in writing" and "shall state the reasons for the decision reached." *Id.* Consistent with the Act, the Federal Acquisition Regulations provide that "[w]hen a default termination is being considered, the Government shall decide which type of termination action to take (i.e., default, convenience ...) only after review by contracting and technical personnel ... to ensure the propriety of the proposed action." 48 C.F.R. § 49.402-3(a). The regulations identify specific factors that "[t]he contracting officer shall consider ... in determining whether to terminate a contract for default," including "[t]he specific failure of the contractor and the excuses for the failure," as well as "[t]he terms of the contract and applicable laws." *Id.* § 49.402-3(f).

Thus, until now, the settled rule was that a default termination cannot be sustained unless the government chose that drastic sanction by exercising informed *discretion* – a choice that necessarily draws upon the contracting officer's expertise with respect to the details of the contractor's performance.

Accordingly, in *Schlesinger v. United States*, 390 F.2d 702 (Ct. Cl. 1968), the Court of Claims (the Federal Circuit's predecessor in government contracts matters) set aside a default termination because "[t]here was no indication of any concern for the contractor or whether a default would be excusable, no consideration of a possible waiver or an extension, no weighing of a convenience termination instead of a default termination." *Id.* at 708-09; *see also Darwin Constr. Co. v. United* States, 811 F.2d 593, 596 (Fed. Cir. 1987) (reaffirming *Schlesinger*); *Hannon Elec. Co. v. United States*, 31 Fed. Cl. 135, 143 (1994) (explaining that "courts will not uphold a default unless the [contracting officer] has carefully examined the contractor's ability to complete the remaining work before the contract completion date"). This requirement dates back to at least 1920. *See Williams Eng'g & Contracting Co. v. United States*, 55 Ct. Cl. 349, 382 (1920).

In conjunction with the requirement of an exercise of discretion, the Federal Circuit and its predecessor court also uniformly confined themselves to review of the factual basis for the default termination that was *actually articulated* by the government at the time of termination. *See* 41 U.S.C. § 605(a). Courts were willing to entertain a reason for default termination not articulated by the contracting officer only when that reason was *legal* rather than factual, and therefore (1) outside of the contracting officer's expertise and (2) beyond the contractor's ability to remedy. *See, e.g., Kelso v. Kirk Bros. Mech. Contractors, Inc.*, 16 F.3d 1173, 1175 (Fed. Cir. 1994) (federal labor standards);

Joseph Morton Co. v. United States, 757 F.2d 1273, 1278 (Fed. Cir. 1985) (fraud); *Pots Unlimited, Ltd. v. United States*, 600 F.2d 790, 793 (Ct. Cl. 1979) (federal regulations and contract provisions); *College Point Boat Corp. v. United States*, 267 U.S. 15, 15-16 (1925) (federal statute).[6]

These now-discarded rules reflected basic principles of administrative law. Where the executive determines the rights of private parties, this Court has always insisted that an agency explain its reasoning, and then has limited judicial review to an examination of the reasons given by the agency in the exercise of its expert authority. *See, e.g.*, *SEC v. Chenery Corp.*, 332 U.S. 194, 196 (1947) ("[A] reviewing court, in dealing with a determination or judgment which an administrative agency alone is authorized to make, must judge the propriety of such action solely by the grounds invoked by the agency. ... [T]he court is powerless to affirm the administrative action by substituting what it considers to be a more adequate or proper basis."); *Motor Veh. Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983). No other approach honors Congress's choice to entrust the decision of certain issues to the executive in the first instance. *See SEC v. Chenery Corp.*, 318 U.S. 80, 88, 94 (1943) (a court "cannot intrude upon the domain which Congress has exclusively entrusted to an administrative agency").

[6] The one exception to this rule is a case that was decided after, and relied upon, the Federal Circuit's decision in the case at hand. *See Empire Energy Mgmt. Sys., Inc. v. Roche*, 362 F.3d 1343, 1357 (Fed. Cir. 2004) (citing Pet. App. 193a-194a).

Here, Congress has entrusted certain decisions to the contracting officer, and required the contracting officer to consider certain issues in rendering his decision. But the Federal Circuit has created a new regime in which the government need not exercise any discretion or assess a contractor's actual performance in deciding on a termination for default, and in which the government can advance any factual basis whatsoever for a court to uphold a termination. Thus, while recognizing that in this case the contracting officer was *ordered* for political reasons to carry out a termination against his will, and acted in such haste that he left a key portion of his termination memo – copied verbatim from a prior memo relating to a different contract – completely blank, the Federal Circuit nevertheless held that because the termination was generally "predicated on contract-related issues, it was within the discretion of the government." Pet. App. 251a; *see also id.* 169a (testimony of contracting officer that he "would not have terminated the contract" had he not been ordered to do so). The court then ruled that it could uphold the default on an "alternative theory" of the facts, even though the government could not "establish that the contracting officer conducted the analysis necessary to sustain a default under [that] alternative theory." *Id.* 29a.

2. As a consequence of this novel and unfair approach, the Federal Circuit has placed billions of dollars in current contracts at risk and created a significant disincentive for contractors to enter into relationships with the government in the future. *See* GAO, *GAO High Risk and Other Major Government*

Challenges: Acquisition Management (government spent $529 billion on private contracts in fiscal year 2008), *available at* http://www.gao.gov/highrisk/challenges/acquisition_management/home_acquisition_management.php; GAO, *Defense Acquisitions: Assessment of Selected Weapons Programs* 10-11 (Mar. 2009) ("Only 28 percent of DOD's major defense acquisition programs currently estimate that they will deliver on time ..., while just under one-half report they will have a delay of 1 year or more in delivery of an initial operational capability.").

The legal requirements that the Federal Circuit has now erased operated as a check on the government's ability to terminate for default – a step that the government already had a great incentive to take, since if the courts overturn a default the sole consequence is conversion to a termination for convenience. *See supra* p. 4. The government can now visit punishment on a contractor without giving notice of what the contractor might actually be doing wrong or what it needs to correct. Indeed, a contractor might correct every problem ever identified by the contracting officer and still suffer a default that is upheld for some *other* reason, dreamed up in the course of litigation. Moreover, that litigation is likely to be protracted and complicated, like the case at hand, since the government can call on its resources to present every imaginable reason for a default, in the hope that one of them will stick.

It is hard to see why any contractor would enter into a difficult or high-stakes contract with the government under these onerous conditions. *See*

Winstar, 518 U.S. at 884 (rejecting rules that "expand[ed] the Government's opportunities for contractual abrogation," but "with the certain result of undermining the Government's credibility at the bargaining table and increasing the cost of its engagements"). Notably, following the Federal Circuit's decision, leading commentators began advising contractors that they should refuse to undertake fixed-price research-and-development contracts like the A-12 contract, a type of contract that the government has increasingly sought to use to develop crucial new technology and to push the envelope in military and other contexts. *E.g.*, Ralph C. Nash, *Fixed-Price Research & Development Contracts: A Risk Too High*, 23 Nash & Cibinic Rep. ¶ 39, at 116 (Aug. 2009). As these commentators have explained, the Circuit's new rules, which make "[d]efault termination ... a viable tactic" when some "higher authority" simply wishes to stop paying, create "too great a risk to take," and so contractors should "adopt the Nancy Reagan solution – *just say no*." *Id.*

3. The problems with the Federal Circuit's approach are well illustrated by the case at hand. The contractors are now subject to a government demand for billions of dollars, and a government refusal to pay billions of dollars for costs the contractors incurred, based on a post-hoc justification. The contractors' past performance, their ability to perform in the future, and their explanations of the government's own fault in creating any performance problems were *never* given due consideration by the contracting officer or

anyone else in the government as part of the hasty decision by the Secretary of Defense to order termination. That is the hallmark of arbitrary and capricious government action. And the Federal Circuit's anemic requirement that the default termination be, in some general way, plausibly "performance-related" is no obstacle to such action, since that requirement can be so readily met in almost every imaginable case.

Moreover, the problems with the government's newly recognized powers are compounded here by the Federal Circuit's decision to significantly weaken the substantive standard for assessing whether the government's after-the-fact rationale is a sufficient one. In 2003, the Federal Circuit correctly held that the government had to prove a "reasonable belief on the part of the contracting officer that there was no reasonable likelihood that the contractor could perform the entire contract effort within the time remaining for performance." Pet. App. 191a. Now, however, the Federal Circuit has greatly loosened this standard, holding that the default can be sustained based on an "ad hoc, factual inquiry" into whether a hypothetical contracting officer could have felt "insecure about the contractors' rate of progress." *Id.* 20a-21a, 27a. This change does away with yet another check on the government's use of its sovereign powers to run roughshod over its counterparties.[7] In conjunction with the other

[7] Petitioner General Dynamics agrees with Petitioner Boeing that the Federal Circuit's decision to change the governing standard in this case is independently worthy of this Court's

changes described above, it gives the government extraordinary latitude to inflict a drastic penalty.

None of this can be reconciled with the basic principle that the government must deal fairly with its contractors and "turn square corners." *Heckler v. Community Health Servs. of Crawford Cty., Inc.*, 467 U.S. 51, 61 n.13 (1984); *see also S&E Contractors, Inc. v. United States*, 406 U.S. 1, 10 (1972). This Court should hear and decide these fundamental issues of government contracts law, which are of extraordinary national importance.

III. The Federal Circuit's Decision Conflicts With the Decisions of Other Circuits on Whether a Panel Can Overrule a Prior Panel in the Same Case Under the Law-of-the-Case Doctrine.

As discussed above, the Federal Circuit is a court of national importance, with sole appellate jurisdiction over patent cases and almost all government contracts cases and, as a result, a profound impact on a wide and important swath of the Nation's economy. Consistency and stability in the Federal Circuit's law is therefore especially important – and a fair and predictable system for dealing with disagreements between different panels of judges is crucial. But the Federal Circuit has long struggled with these issues, and its most recent decision in this case creates additional inconsistency and instability.

review, and joins the request for review of that issue. *See* Boeing Pet. (filed Apr. 23, 2010).

In that decision, the Federal Circuit determined that under the law-of-the-case doctrine – which permits alteration of prior rulings under certain circumstances – a panel has the authority to disregard Circuit precedent by overruling a prior panel decision that was issued in the course of the same case. That decision not only was outcome-determinative here, but also undermines the confidence of all Federal Circuit litigants. Moreover, it directly conflicts with the rule in a number of other circuits, which have held that the "law of the circuit" doctrine, a bedrock principle of *stare decisis* under which only an *en banc* court can overrule a panel decision, trumps the law-of-the-case doctrine. This Court, which has the "power to supervise the administration of justice in the federal courts," *Western Pacific Railroad Corp. v. Western Pacific Railroad Co.*, 345 U.S. 247, 260 (1953), should step in to ensure consistency in the Federal Circuit and to resolve this split among the circuits.

In its 2003 panel decision in this case, the court of appeals applied its longstanding precedent and unequivocally ruled that the government could not sustain its default termination claim on a mere showing that the contractors were likely to be behind schedule on an interim contract deadline. Rather, the court held, the government would have to prove that the contracting officer had a reasonable belief that there was no reasonable likelihood of timely completion of the "entire contract effort" – a standard that required a valid deadline for contract completion. Pet. App. 193a, 195a-197a, 211a; *see also id.* 195a-196a (acknowledging that the

contractors contended no such final deadline existed). On remand, the trial court found that the government had disestablished the contract completion date and never set a new one. *Id.* 164a. The 2009 panel agreed. *Id.* 14a. Yet it discarded the 2003 panel's legal standard, shifting to an amorphous "ad hoc, factual inquiry." *Id.* 20a-21a. Amazingly, the new panel all but acknowledged that it had altered the governing standard in service of a particular result, suggesting that a victory by the contractors would be an "injustice," and that the law-of-the-case doctrine therefore authorized a departure from the prior panel ruling, even absent an intervening change in fact or law. *Id.* 27a n.4.

In the Federal Circuit, therefore, if a panel considers an earlier panel decision in the same case to be unjust or erroneous, the later panel can simply set it aside. Other circuits have reached exactly the opposite result. *See United States v. 162.20 Acres of Land*, 733 F.2d 377, 379 (5th Cir. 1984); *United States v. Washington*, 593 F.3d 790, 798 n.9 (9th Cir. 2010); *United States v. Alaw*, 327 F.3d 1217, 1220 (D.C. Cir. 2003); *see also Swipies v. Kofka*, 419 F.3d 709, 714 (8th Cir. 2005); *Schiavo ex rel. Schindler v. Schiavo*, 403 F.3d 1289, 1292 (11th Cir. 2005); *Craft v. United States*, 233 F.3d 358, 363, 369 (6th Cir. 2000), *rev'd on other grounds*, 535 U.S. 274 (2002); *Cohen v. Brown University*, 101 F.3d 155, 169 (1st Cir. 1996); *Howard v. Mail-Well Envelope Co.*, 90 F.3d 433, 435 (10th Cir. 1996).

For instance, in *162.20 Acres of Land*, the Fifth Circuit rejected a plea to overturn a prior panel's holding in the same case. The court declared that

"[i]n this circuit ... the law-of-the-case doctrine is supplanted by our firm rule that one panel cannot disregard the precedent set by a prior panel even though it perceives error in the precedent." 733 F.2d at 379.

The Ninth Circuit applies the same rule. In *Washington*, the court explained that it was required to hear an appeal *en banc* because "even if the panel could have revisited [the prior panel's opinion in the same case] under one of the exceptions to law of the case ... it still would have been bound by that published opinion as the law of the circuit." 593 F.3d at 798 n.9 (citing *Old Person v. Brown*, 312 F.3d 1036, 1039 (9th Cir. 2002)).

Had the Federal Circuit taken the same approach, the 2009 panel would have ruled for the contractors. Indeed, the 2009 panel itself recognized that the contractors would have prevailed under the standard the previous panel had mandated. Pet. App. 27a n.4. But the decision of a later panel to overrule the earlier one has allowed the government to claim a right to billions of dollars from the contractors – an extraordinary and improper result.

The injustice was heightened here by procedural unfairness that is a risk in any system in which a later panel may overrule an earlier panel in the same case. Having litigated under the 2003 mandate for years, the contractors had no opportunity to present evidence or argument under the newly announced "ad hoc" test – even though that is a test under which the contractors also could have prevailed. Rather, the Federal Circuit made its own

factual findings under the new test on the basis of the existing record, disregarding contrary evidence and conflicting trial court findings in the course of doing so.[8] The temptation to put an end to long-running litigation in this way – even at the expense of a fair hearing on remand for the losing litigant – is obviously great, especially when the deciding panel knows that any *subsequent* panel would be able to change the governing law in the case yet *again*. Accordingly, under the Federal Circuit's approach, these problems are likely to arise in future cases as well.

But that is far from the only concern raised by the Federal Circuit's departure from the "law of the circuit" rule of *stare decisis* followed by other courts of appeals. That rule serves the important purpose of "establish[ing] the orderly development of federal law" so that it is "at least uniform within a single Circuit." 18B Charles Alan Wright et al., *Federal Practice & Procedure* § 4478.2, at 727 (2d ed. 2002). In contrast, the Federal Circuit's exception "significantly undermine[s]" the "stability of the law" in that court. *United States v. Bordeaux*, 400 F.3d 548, 554 (8th Cir. 2005). Now, losing litigants have every incentive to go over the same ground twice, hoping that the second time they will draw a panel that is more favorable to their position. *Compare Vasquez v. Hillery*, 474 U.S. 254, 265-66 (1986) (explaining that *stare decisis* is intended to "permit[]

[8] Petitioner General Dynamics agrees with Petitioner Boeing that this procedural issue is independently worthy of this Court's review, and joins the request for review of that issue. *See* Boeing Pet. (filed Apr. 23, 2010).

society to presume that bedrock principles are founded in the law rather than in the proclivities of individuals"). And no party – or, for that matter, non-party – can count on the fact that a legal test set forth in a panel decision will stand (absent an intervening legislative enactment or ruling by this Court) unless and until it is considered and altered by the *en banc* court, with the full participation of the members of the original panel. The result is that confidence in the rule of law is undermined, and the Circuit's law thrown into disarray.

The Federal Circuit can ill afford these damaging consequences. Because it is the only circuit that hears patent cases and (with minor exceptions) government contracts cases, consistency among that court's panel decisions is especially important – and, indeed, one of Congress's express purposes in establishing the court was fostering predictability and uniformity in these areas of the law. *See* Federal Courts Improvement Act of 1982, Pub. L. No. 97-164, 96 Stat. 25. Yet consistency and predictability are areas in which the Federal Circuit already struggles significantly, as many commentators have recognized. *See, e.g.*, Paul M. Janicke, *On the Causes of Unpredictability of Federal Circuit Decisions in Patent Cases*, 3 Nw. J. Tech. & Intell. Prop. 93, 93 (2005) (stating that the "court has been increasingly criticized for inconsistency"); Matthew F. Weil & William C. Rooklidge, *Stare Un-Decisis: The Sometimes Rough Treatment of Precedent in Federal Circuit Decision-Making*, 80 J. Pat. & Trademark Off. Soc'y 791, 793 (1998).

This Court should not leave in place a rule that exacerbates these problems, places the Federal Circuit at odds with its sister circuits on an important procedural issue, and subjects the contractors to a government demand for a multi-billion-dollar forfeiture.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX

Supreme Court, U.S.
FILED

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No. OFFICE OF THE CLERK

IN THE
Supreme Court of the United States

GENERAL DYNAMICS CORPORATION,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

On Petition For A Writ Of Certiorari To The
United States Court Of Appeals
For The Federal Circuit

PETITIONER'S APPENDIX

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April 23, 2010

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APPENDIX A

United States Court of Appeals,
Federal Circuit.

McDONNELL DOUGLAS CORPORATION,
Plaintiff-Appellant,
and
General Dynamics Corporation,
Plaintiff-Appellant,
v.
UNITED STATES,
Defendant-Appellee.

Nos. 2007-5111, 2007-5131.

June 2, 2009.
Rehearing and Rehearing En Banc Denied
Nov. 24, 2009.*

MICHEL, Chief Judge.

This case arises from the government's default termination in 1991 of a contract between the United States Navy ("the government") and two contractors, McDonnell Douglas Corporation ("MDC") and General Dynamics Corporation ("GD") (collectively "contractors") to develop a carrier-based stealth aircraft, the A-12 Avenger. The contractors challenge the judgment of the Court of Federal Claims in favor of the government. *McDonnell Douglas Corp. v. United States,* 76 Fed. Cl. 385 (2007) (" *McDonnell Douglas XIII* "). We heard oral

* Circuit Judge Bryson did not participate in the vote.

argument on December 3, 2008. Because the overall evidence of record supports a conclusion that the government was justified in terminating the contract for default, we affirm.

I. BACKGROUND

This American version of *Jarndyce and Jarndyce* has entered its eighteenth year of litigation. The detailed facts have been repeated many times previously. *See, e.g., McDonnell Douglas XIII; McDonnell Douglas Corp. v. United States*, 323 F.3d 1006 (Fed. Cir. 2003) *("McDonnell Douglas XII"); McDonnell Douglas Corp. v. United States*, 50 Fed. Cl. 311 (2001) *("McDonnell Douglas XI");* and *McDonnell Douglas Corp. v. United States*, 182 F.3d 1319 (Fed. Cir. 1999) *("McDonnell Douglas X").* As we are writing what necessarily will become "*McDonnell Douglas XIV,*" we will only provide a summary of relevant facts here.

A. The A-12 Contract

In January 1988, the Navy awarded the contractors a fixed-price research and development contract for the A-12 stealth aircraft. The full-scale engineering and development ("FSD") contract was structured as an incrementally funded, fixed-price incentive contract with a ceiling price of $4,777,330,294. The contract incorporated by reference *Federal Acquisition Regulation (FAR) 52.249-9* Default provision (Fixed-Price Research and Development), which provides in relevant part:

> (a)(1) The Government may ... by written Notice of Default to the Contractor,

> terminate this contract in whole or in part if the Contractor fails to-
>
> ...
>
> (ii) Prosecute the work so as to endanger performance of this contract (but see paragraph (a)(2) of this clause);
>
> ...
>
> (2) The Government's right to terminate this contract under subdivisions (a)(1)(ii) and (iii) of this clause may be exercised if the Contractor does not cure such failure within 10 days (or more, if authorized in writing by the Contracting Officer) after receipt of the notice from the Contracting Officer specifying the failure.

48 C.F.R. § 52.249-9 (1984).

Under the contract, the contractors were to design, manufacture, and test eight A-12 prototypes according to a specified schedule, with the first aircraft to be delivered in June 1990 (the "first flight" date) and the remaining seven to be delivered monthly through January 1991. The contractors were to conclude their testing of the aircraft by April 1993, the completion time of the Navy's technical evaluation program ("TCHEVAL"). The contractors would also support the Navy's evaluation of the aircraft and further provide training support for three years after delivering training equipment to the Navy in June 1993. In addition, the contract gave the Navy the option to purchase four production lots of aircraft. In May 1990, the Navy exercised its

option on Lot I for six aircraft to be delivered between June 1991 and May 1992.

B. Modification of the A-12 Contract

From the start, the contractors encountered difficulties in performing the contract, including meeting the contract schedule and keeping the aircraft weight within specifications. *McDonnell Douglas XI I,* 323 F.3d at 1011. Two weeks before the first flight date, the contractors reported to the Navy that the projected first flight date would be July-September 1991, instead of June 1990 as originally agreed, and the remainder of the contract work would be delayed a corresponding twelve to fourteen months. They also predicted that the cost of completing the contract would exceed the ceiling price so substantially that it would be "unacceptable" to the contractors. The contractors asserted that a fundamental problem with the FSD contract was its fixed-price structure and proposed that the contract be modified.

At the end of June 1990, the contractors missed the first flight date. The Navy did not terminate the contract. Instead, the contracting officer sent a letter to the contractors in July, expressing "serious concern" regarding the deficient performance under the contract. He warned that the contractors' failure to meet the first flight date "could jeopardize performance of the entire [contract] effort." He also asked for the contractors' plan to meet the rest of the original schedule as well as their proposal for contract revision.

As the parties failed to reach an agreement, on August 17, 1990, the Navy unilaterally issued a contract modification, P00046, which revised the prototype aircraft delivery dates but left Lot I and later milestones intact. The delivery schedules are:

	Aircraft Number	Original Delivery Date	P00046 Modified Delivery Date
Prototype	1	June 1990	December 1991
	2	July 1990	February 1992
	3	August 1990	June 1992
	4	September 1990	August 1992
	5	October 1990	September 1992
	6	November 1990	November 1992
	7	December 1990	December 1992
	8	January 1991	February 1993
Lot 1	9	June 1991	
	10	August 1991	
	11	October 1991	
	12	December 1991	
	13	March 1992	
	14	May 1992	

C. Performance after contract modification

After the contract modification, more problems arose concerning the performance of the contract. During the months leading to termination, the contractors' internal schedules showed that they would not meet the P00046 modified first flight date

in December 1991. *McDonnell Douglas XIII,* 76 Fed. Cl. at 401. Instead, they projected three more months' delay with the first flight date in March 1992. By December 1990, the contractors' "confidence in the March 1992 flight date [was further] reduced." They believed that such a date was achievable "only after significant changes."

At the same time, the contractors continued operations, spending $120-150 million of their own money every month. *McDonnell Douglas XIII,* 76 Fed. Cl. at 427. In November 1990, the contractors submitted a formal request to the Navy to restructure the contract as a cost-reimbursement type contract. *McDonnell Douglas X,* 182 F.3d at 1322.

D. The Termination

The contractors' continued difficulties in performing the contract led the Department of Defense and the Navy to question the viability of the project. On Friday, December 14, 1990, then-Secretary of Defense Dick Cheney directed the Secretary of the Navy to show cause by January 4, 1991, why the A-12 program should not be terminated.

The following Monday, December 17, the Navy issued a cure notice to the contractors, stating that the government considered the contractors' performance under the contract "unsatisfactory." In particular, the cure notice stated that the contractors had "failed to fabricate parts sufficient to permit final assembly in time to meet the schedule for delivery," and had "failed to meet specification

requirements." The letter asserted that "these conditions [were] endangering performance of [the] contract," and that unless these conditions were cured by January 2, 1991, the government might terminate the contract for default.

In the following days, high-level meetings occurred between the responsible government personnel and the contractors. *McDonnell Douglas X*, 182 F.3d at 1323. During these meetings, the contractors asserted that they could not "get there if [they didn't] change the contract," and that it "got to get reformed to a cost type contract or [they could not] do it." When asked by the government if they could "correct deficiencies to provide an aircraft that meets the requirements," the contractors replied that "all deficiencies cannot be corrected.... Mother [N]ature won't allow correction of all defects. We'll do the best we can and the Navy has to decide if that's good enough."

On January 2, 1991, in responding to the cure notice, the contractors admitted that they would "not meet delivery schedules or certain specifications of the original contract, or the revised FSD delivery schedule." However, they denied that they were in default because, in their view, the delivery schedules were invalid. They asserted that "the fundamental factual assumptions of the original contract, with respect to schedule and achievability of certain specification requirements, were gravely mistaken," and therefore, "the schedules and certain other specification requirements, such as weight, were impossible to satisfy." The contractors concluded that "[i]n these circumstances, there [was] not an

enforceable schedule or specifications against which to measure their performance." They further declared that compliance with the government's demand to cure by January 2, 1991 was "unachievable."

However, the contractors stated that they were "fully committed to the success of the [A-12] Program." They again submitted their proposal to restructure the contract to a cost reimbursement contract. In exchange for that restructuring, the contractors would absorb a $1.5 billion fixed loss and would waive their claims for equitable adjustment.

On January 7, 1991, Rear Admiral William Morris, the contracting officer at the time, issued a termination letter to the contractors stating that the government was terminating the A-12 contract due to the contractors' default. A few weeks later, the Navy sent a letter to the contractors demanding the return of approximately $1.35 billion in unliquidated progress payments under the terminated contract. *McDonnell Douglas X,* 182 F.3d at 1324.

II. LITIGATION HISTORY

A. The First Round

In June 1991, the contractors sought relief in the Court of Federal Claims under the Contract Disputes Act, 41 U.S.C. § 609(a), requesting that the court: (1) grant the contractors' equitable adjustment claims, (2) convert the government's termination for default into a termination for convenience, (3) deny the government's demand for return of progress payments, (4) award the contractors costs and a reasonable profit under the contract, (5) award the

contractors settlement expenses, and (6) award damages for breach of contract.

After several years of litigation, the Court of Federal Claims ruled that the government's default termination was invalid. *McDonnell Douglas Corp. v. United States*, 35 Fed. Cl. 358, 368-71 (1996) ("*McDonnell Douglas IV*"). It found that the contracting officer failed to exercise "reasoned discretion" before the default termination because Secretary Cheney's actions effectively forced the Navy to terminate the A-12 contract for default. *Id.* at 369-71. Therefore, it vacated the government's termination for default and converted it into a termination for convenience. *Id.* at 361. The court ultimately denied the government's claim for return of $1.35 billion in unliquidated progress payments, and entered judgment of approximately $1.2 billion in favor of the contractors. *McDonnell Douglas Corp. v. United States,* 40 Fed. Cl. 529, 555-56 (1998) ("*McDonnell Douglas IX*").

On appeal, we reversed, holding that because the termination for default was related to the contractors' performance, it was within the discretion of the government. *McDonnell Douglas X,* 182 F.3d at 1321. We remanded the case for the trial court to determine whether the default termination was justified. *Id.*

B. The Second Round

After a six-week trial on remand, the Court of Federal Claims ruled in favor of the government. *McDonnell Douglas XI,* 50 Fed. Cl. at 319. The court sustained the default termination based solely on the

contractors' failure to meet the December 1991 first flight date. *Id.* at 315-19. It declined to base its determination of justified default on the contractors' alleged financial inability to perform the contract, anticipatory repudiation, and failure to comply with weight and other specification requirements. *Id.* at 319-24. The court also rejected the contractors' arguments that the unilateral schedule was unreasonable and therefore unenforceable, or, if enforceable then the Navy waived the unilateral schedule and first flight date of December 1991; that the contract was commercially impossible to perform; and that the Navy had to disclose its alleged superior knowledge despite the assertion of the state secrets privilege. *Id.* at 324-26. The court then entered judgment in favor of the government. *Id.* at 326.

On appeal, we affirmed the trial court's determination that the unilateral schedule imposed by the government was enforceable and not waived, that the Military and State Secrets privilege precluded litigation of the contractors' "superior knowledge" claim, and that the government's claim for progress payments was not at issue in the case. *McDonnell Douglas XII,* 323 F.3d at 1018-24. However, we held that the trial court misapplied the controlling standard in determining whether the default termination was justified. *Id.* at 1012-14. Therefore, we again vacated and remanded. *Id.*

Specifically, we stated that a default termination did not require "absolute impossibility of performance or a contractor's complete repudiation or abandonment." *Id.* at 1015. On the other hand, the government cannot justify a default termination

"based solely on a contractor's concerns about meeting a contractual schedule milestone or specification requirements." *Id.* Instead, the government must establish by a preponderance of the evidence of a "reasonable belief on the part of the contracting officer that there was no reasonable likelihood that the contractor could perform the entire contract effort within the time remaining for contract performance." *Id.* at 1016. (citing *Lisbon Contractors, Inc. v. United States,* 828 F.2d 759, 765 (Fed. Cir. 1987)).

C. The Third Round

On remand, the Court of Federal Claims stated as follows:

> The case turns on whether the Circuit's remand meant for the clauses, "entire contract effort" and "contract completion date" to mean exactly what they appear to mean-the contractors' expansive view; or whether the remand permits our use of a more compact yardstick-coinciding with the Government's restricted view. The Government did not establish a contract closing date and the contracting officer did not conduct a *Lisbon* analysis prior to termination.

McDonnell Douglas XIII, 76 Fed. Cl. at 437 n.92. The court concluded that the government could not "prevail if the law require[d] an enforceable contract completion date at termination," but went on to state that the government's "burden of proof [did] not nec-

essarily require the Government to provide a completion date for the entire contract effort." *Id.* at 388.

Based on its understanding that we "implied in this case that a court may choose a reasonable period of performance to use as a measure of progress on the contract," *id.* at 420, the court found that the Navy's unilateral modification, P00046, was a yardstick that "enable[d] the court to consider the contractors' progress in light of factors that are probative of their ability and willingness to perform," *id.* at 389. Using P00046 as the yardstick and considering "all of the relevant facts and testimony," *id.* at 421, including mitigating factors for the contractors, the court concluded that the overall evidence of record supported a conclusion that the government was justified in terminating the contract for failure to make progress, *id.* at 430.

In addition, the trial court stated that the judgment in the case mooted the government's alternative argument that the contractors did not provide adequate assurances to the contracting officer after receiving the notice to cure. *Id.* at 434.

The contractors timely appealed. We have jurisdiction pursuant to 28 U.S.C. § 1295(a)(3).

III. DISCUSSION

A. Standard of Review

Whether the government is justified in terminating a contract for default is a question of law based on factual underpinnings. *McDonnell Douglas X*, 182 F.3d at 1325. We review issues of law de novo, without deference to the trial court.

McDonnell Douglas XII, 323 F.3d at 1012 (citation omitted). However, we will not disturb the trial court's factual findings, such as its evaluation of evidence of default, unless they are clearly erroneous. *Id.*

B. Analysis

1. Termination for failure to make progress in the absence of a contract completion date

In *McDonnell Douglas XII*, we quoted the language from *Lisbon in toto* and directed the Court of Federal Claims to determine "the performance required by the contract[1] and *the contract completion date*." 323 F.3d at 1018 (emphasis added, footnote added). We acknowledge that this specific instruction, if read literally, turns out to be difficult to apply. This is largely due to the unique facts of this case and the disadvantage we faced last time when deciding the case without the benefit of sufficient fact findings from the trial court. *See id.* at 1014.

[1] Generally, obligations arising from the exercise of an option are part of a new contract only when the option was the principal subject matter of the bargain, *i.e.*, an option contract. *Alliant Techsystems, Inc. v. United States*, 178 F.3d 1260, 1275 (Fed. Cir. 1999) (citing 3 Eric Mills Holmes, *Corbin on Contracts* § 11.1 (1996)). In this case, because the option to purchase Lot I production aircraft is not the principal subject matter of the original bargain, it is properly considered as part of the original A-12 contract between the contractors and the government. Thus, "the performance required by the contract" includes the design, manufacturing, and testing of the eight prototype planes under the FSD contract, the manufacturing and

The difficulty in strictly applying the *Lisbon* test lies in the critical fact that P00046 revised the prototype aircraft delivery dates but left Lot I delivery dates unchanged. As such, there is an overlap between the modified delivery schedule for the eight prototype aircraft and the original delivery schedule for the Lot I production aircraft. *See* Delivery Schedules, *supra*. The government insists that the Lot I schedule remains in effect because that portion of the original contract was not modified by P00046. However, "[t]he A-12 contract was designed as a long-term research and development effort, structured so that each period of performance built upon preceding work." *McDonnell Douglas XIII,* 76 Fed. Cl. at 432. Because the eighth test plane would serve as the prototype for the Lot I aircraft, the contractors could not have delivered Lot I aircraft according to the original schedule as that would require delivering the production aircraft prior to the prototype planes. Therefore, we agree with the Court of Federal Claims that the "[a]pplication of the contract in [the] manner [advocated by the government] would be nonsensical." *McDonnell Douglas XIII,* 76 Fed. Cl. at 432. It follows that the contract, as modified by P00046, does not provide a definite contract completion date.[2]

testing of the six Lot I production aircraft, and other testing and supporting of the project.

[2] The contractors offered legal principles, such as judicial estoppel and waiver, to support this point. We do not believe it is necessary to reach those arguments. Whether the contract has a completion date is a question of fact. Common sense in this case dictates the conclusion that "[t]he overlapping schedule

The contractors would have us apply the *Lisbon* test literally and hold that the absence of a contract completion date *per se* precludes the government from ever justifiably terminating a contract for failure to make progress. We cannot adopt such a broad categorical rule. The propriety of such a default termination, even though ultimately a question of law, is a fact-sensitive inquiry. The *Lisbon* test requires the contracting officer's *reasonable* belief that there was no *reasonable* likelihood of timely completion. *Lisbon,* 828 F.2d at 765. Therefore, it is inevitable that some case-by-case adjudication is required.

To be sure, just as the prior panel did, we reaffirm that the test formulated in *Lisbon* is a correct standard for determining whether a default termination for failure to make progress is justified. However, this test was announced in view of the specific facts presented in that case, where there was a definite contract completion date. *Lisbon,* 828 F.2d at 761, 762. It did not address the situation where, as in the present case, the contract does not specify a fixed completion date. *See United States v. Alaska S.S. Co.,* 253 U.S. 113, 116, 40 S. Ct. 448, 64 L. Ed. 808 (1920) (stating that a court "will determine only actual matters in controversy essential to the decision of the particular case before it," and that it "is not empowered to decide ... abstract propositions ... which cannot affect the result as to the thing in

offered by the Government as a basis for assessing default is unreasonable and likely unenforceable." *McDonnell Douglas XIII,* 76 Fed. Cl. at 432.

issue in the case before it"). As such, the *Lisbon* standard could not be literally applied in every default termination for failure to make progress case.

We are confident that *Lisbon* does not, as the contractors argue, foreclose a court's review of a default termination for failure to make progress merely because of an unascertainable contract completion date. This is evident from *Lisbon* itself, in which the court approved the Claims Court's citation and interpretation of *Universal Fiberglass Corp. v. United States,* 210 Ct. Cl. 206, 537 F.2d 393, 397 (1976).[3] *Lisbon,* 828 F.2d at 765.

Universal Fiberglass involved a supply and service contract for more than 12,000 mail delivery trucks. 537 F.2d at 394. The contractor in that case repeatedly failed to meet the installment delivery schedule, even after several extensions of time. *Id.* at 394-95. It closed down almost all of the production lines and laid off most of its labor force. *Id.* at 395. Meanwhile, a government audit showed that the contractor was insolvent. *Id.* Time and again, the government asked the contractor to furnish its proposed revised delivery schedule, but to no avail. *Id.* The government issued a Preliminary Notice of Default and gave the contractor ten days to cure all of its defaults. *Id.* at 396. After the contractors waived its rights to the full ten-day

[3] *Universal Fiberglass* was also cited with approval by the previous two panels in deciding the present case. *See McDonnell Douglas X,* 182 F.3d at 1328; *McDonnell Douglas XII,* 323 F.3d at 1015

notice period, the government promptly terminated the contract for failure to make progress. *Id.*

The Court of Claims held that the contract was properly terminated for failure to make progress. *Id.* The court found that in the absence of a delivery schedule, *i.e.*, the contract completion date, the "cure notice" served the purpose of advising the contractor when the time for default has been reached. *Id.* at 398. The court reasoned:

> The contractor had already been asked to submit a new delivery schedule and had not done so. Nor had the contracting officer learned, from the contractor or any other source, any information to lead him to believe that deliveries would or could ever be resumed. In such circumstances, a unilateral delivery schedule prescribed by him would have been an exercise in futility, except for forensic purposes, should we be so foolish as to give the absence of such a schedule any legal significance or weight.

Id.

We realize that the facts in *Universal Fiberglass* are not exactly the same as in the present case. First, the difficulties in designing and manufacturing stealth aircraft are incomparable to those in making small three-wheeled mail delivery trucks. More importantly, as the contractors correctly point out, in *Universal Fiberglass,* the contractor "was making no progress at all, had never manufactured a vehicle under the new specifications it had agreed to, did not have the necessary parts and could not obtain them

and had allowed its labor force to wither away." *Id.* at 398. In contrast, in the present case, "[d]espite delays, the contractors continued operations. They were spending $120 to $150 million of their own money every month. They were committed to performing the A-12 contract until the date of termination." *McDonnell Douglas XIII,* 76 Fed. Cl. at 427.

However, the contractors' commitment to performing the contract was not without conditions. Starting from as early as June 1990, the contractors had asserted that "the A-12 contractual schedule [was] not achievable and need[ed] to be changed." They also predicted that the cost of completing the contract would exceed the ceiling price so substantially that it would be "unacceptable" to the contractors. Insisting that the A-12 project could not "be accomplished under a fixed price type contract without [solving] the financial, schedule and specification problems," the contractors proposed that the contract be modified. The contractors maintained this position throughout their performance of the A-12 contract.

After missing the original first flight date, "[t]he contractors were working to an aggressive schedule, but they would not sign up for one." *McDonnell Douglas XIII,* 76 Fed. Cl. at 399. Because the contractors rejected the government's proposal of a bilateral modification of the contract, the government imposed the unilateral modification of the delivery schedule for the prototype airplanes, P00046, "as a first step in achieving the overall

delivery schedule." *McDonnell Douglas XIII,* 76 Fed. Cl. at 400.

P00046 extended the first flight date from June 1990 to December 1991. The contractors' projected delivery date, however, further slipped away. "Six months prior to termination, the contractors projected a twelve to fourteen-month delay in first flight [June-August 1991]. By termination, the contractors' expectations extended first flight to March 1992." *McDonnell Douglas XIII,* 76 Fed. Cl. at 422. In fact, by December 1990, the contractors' confidence in even the March 1992 flight date was reduced. They believed that such a date was achievable "only after significant changes." As the trial court found, "Navy officials ... could not predict when the contractors would deliver first flight." *McDonnell Douglas XIII,* 76 Fed. Cl. at 401.

As the contractors themselves emphasize, "one cannot test an aircraft before it has been built, nor build a production airplane before developing its prototype." Therefore, without the timely delivery of the prototype airplanes, there would be no basis for the government to prescribe a new delivery schedule for Lot I aircraft. In this sense, similar to the Court of Claim's opinion in *Universal Fiberglass,* we believe requiring the contracting officer to artificially reset the contract completion date would have been "supererogatory," "except for forensic purposes." *See Universal Fiberglass,* 210 Ct. Cl. at 217, 537 F.2d 393. Therefore, we agree with the trial court that this case is similar to *Universal Fiberglass* in that

> a schedule is not necessary because the cure notice supplants the schedule and serves a similar function. The cure notice lets a contractor know that even if performance or delivery is not yet due, the contracting officer believes the contractor may not be making sufficient progress to complete the contract on time. The burden is then on the contractor to advise the Government how it will complete the project on time, according to contract requirements.

Id. at 419.

One could analogize the *per se* rule advocated by the contractors to an injunction against the government. In granting or denying an injunction, a court follows traditional equitable principles and "balances the conveniences of the parties and possible injuries to them" to arrive at a "nice adjustment and reconciliation" between the competing claims. *Weinberger v. Romero-Barcelo,* 456 U.S. 305, 312, 102 S. Ct. 1798, 72 L. Ed. 2d 91 (1982). When a government contract is terminated, there are two interests at issue-the contractor's interest in holding the government to its obligation to carry out the contract, and the government's interest in not wasting taxpayer dollars. The contractors in this case, however, would have us enjoin the government from ever terminating a contract for failure to make progress based on a single factor-the contract lacks a set completion date. We reject such a *per se* rule because it serves only the contractors' interest. Instead, we favor an ad hoc,

factual inquiry that allows careful examination and weighing of all relevant circumstances. *See McDonnell Douglas XII,* 323 F.3d at 1014 (stating that "[i]n determining whether a default termination was justified, a court must review the evidence and circumstances surrounding the termination, and that assessment involves a consideration of factual and evidentiary issues").

In fact, in our 2003 opinion, we provided the same guidance, stating that to determine whether a default termination is justified, "the trial court should focus on the events, actions, and communications leading to the default decision in ascertaining whether the contracting officer had a reasonable belief that there was no reasonable likelihood of timely completion." *McDonnell Douglas XII,* 323 F.3d at 1017. Of course, in some cases, it is possible that a conclusion drawn from a comparison of the entire contract effort and the time remaining for contract performance is so clear that it becomes dispositive. *See Lisbon,* 828 F.2d at 765. However, in cases such as the present one, where such a comparison is inapplicable, the court must examine other factors, including the contractor's failure to meet progress milestones, its problems with subcontractors and suppliers, its financial situation, and its performance history. *See McDonnell Douglas XII,* 323 F.3d at 1017. Only after analyzing the totality of the circumstances can a court determine whether a contractor failed to "[p]rosecute the work so as to endanger performance" of the contract. *See*48 C.F.R. § 52.249-9.

2. Default termination of the A-12 contract

It is true that the A-12 contract, as modified by P00046, lacks a definite contract completion date. However, this single factor, even though important, is insufficient to support the contractors' contention that the government cannot sustain the default termination. A court must also take into account other relevant facts and testimony in deciding whether the default termination was justified.

In *Lisbon,* we held that the government bears the burden of justifying the propriety of a default termination. 828 F.2d at 765. We also stated that "the contracting officer's termination decision [must] be based on tangible, direct evidence reflecting the impairment of timely completion." *McDonnell Douglas XII,* 323 F.3d at 1016 (citing *Lisbon,* 828 F.2d at 766). The direct evidence includes the contractors' "statements that they could not meet the contract specifications, the contract delivery schedule, nor complete performance at the specified contract price." *Id.* at 1013 (quoting *McDonnell Douglas X,* 182 F.3d at 1332). The direct evidence also includes the "contracting officer's testimony and contemporaneous documents." *Id.* at 1016. The Court of Federal Claims made detailed factual findings based on the evidence. *McDonnell Douglas XIII,* 76 Fed. Cl. at 422-30. After reviewing the record, we see no clear error. Therefore, we only highlight a few important aspects here.

a. Contractors' performance history and failure to meet progress milestones

The contractors missed several milestones under the original contract, the most significant of which, of course, is the June 1990 first flight date. They also missed the July 1990 delivery date for the second prototype airplane. More tellingly, after the government unilaterally modified the contract through P00046, and in fact, in their response to the cure notice, the contractors unequivocally stated that they would not meet the revised delivery schedule for the eight prototype airplanes. Instead, they projected that the first flight date would be in March 1992, three months after the date imposed in P00046. By December 1990, the contractors were only "50%" confident in this date, believing it was achievable "only after significant changes."

The contractors and the *amicus curiae* argue that if we uphold the default termination here, the government may terminate for failure to make progress a contract for any minor slippage in meeting any insignificant interim milestone. This is an exaggeration. First of all, due to the sequential "building block" structure of the A-12 contract, delivery of the prototype airplanes is not just any milestone. It is certainly not an insignificant milestone. Quite to the contrary, it is clearly one of the most important milestones in the entire contract. This is because, as the contractors admit, "one cannot test an aircraft before it has been built, nor build a production airplane before developing its prototype."

Second, the delay in the delivery schedule is hardly just a minor slippage. The A-12 contract provided the June 1990 first flight date. In other words, it provided the contractors thirty months from the contract award time (January 1988) to deliver the first prototype plane. P00046, in extending the first flight date to December 1991, gave the contractors 60 percent more time to reach this significant milestone. Yet, the contractors, even though at first predicting that they would, concluded that they could not meet this schedule. In fact, they were not even sure if they could deliver in March 1992. According to the contractors' own estimate, even assuming they could meet the March 1992 first flight date, they would not complete the design, manufacturing, and testing of the aircraft until July 1995, two years and three months after the April 1993 TCHEVAL deadline specified in the original contract.

More importantly, we are not upholding the default termination "based solely on a contractor's concerns about meeting a contractual schedule milestone." *McDonnell Douglas XII,* 323 F.3d at 1015 (citing *Lisbon,* 828 F.2d at 765). As we explained above, the contractors' failure to meet progress milestones is one factor to be considered in the totality-of-the-circumstances analysis. In this respect, we agree with the trial court that

> [m]issed milestones "indicate a pattern of nonperformance and delay which should not be ignored. Although not justifications for default in themselves, they provide a context for understanding and evaluating

> plaintiff's continued problems." Such information should be relevant if we consider whether a reasonable contracting officer might reasonably have been concerned about [the contractors'] ability to complete the contract on time.

McDonnell Douglas XIII, 76 Fed. Cl. at 426 (quoting *Universal Fiberglass,* 537 F.2d at 397).

b. Contractors' financial situation

Another piece of relevant information we consider when reviewing a default termination is the contractors' financial situation. "The cost to complete a contract-more particularly, the inability of a contractor to perform a contract at the specified contract price ... [is a] fundamental element[ ] of government contracts and [is] related to contract performance; as such, [it is] highly relevant to the question of default." *McDonnell Douglas X,* 182 F.3d at 1328.

The A-12 contract as initially awarded had a target contract price of $ 4,379,219,436 and a ceiling price of $ 4,777,330,294. In June 1990, the contractors proposed that the fixed-price contract be modified because the cost of completing the contract would exceed the ceiling price so substantially that it would be "unacceptable" to the contractors.

The contractors repeatedly insisted on restructuring the contract from a fixed-price contract to a cost-reimbursement type contract. Even during the high-level negotiation meetings following the government's issuance of the cure notice, Mr. John McDonnell, the CEO of MDC, asserted that the

contractors "can't get there if we don't change the contract," and that the contract "has got to get reformed to a cost type contract or we cannot do it." In their January 2, 1991, written response to the cure notice, the contractors again submitted their proposal to restructure the contract to a cost reimbursement contract. In exchange for that restructuring, the contractors would absorb a $1.5 billion fixed loss and would waive their claims for equitable adjustment. The sizeable concession the contractors were willing to make further illustrates the grave inadequacy of the contract price.

Of course, the difficulty in the contractors' financial situation, in and of itself, may not be sufficient to justify the default termination. *See McDonnell Douglas XI*, 50 Fed. Cl. at 320-21 (ruling that the contractors' financial condition "was not endangering performance of the A-12 contract"). However, in this case, "inadequate financing is not collateral [because] it pervades the entire contract." *Universal Fiberglass*, 210 Ct. Cl. at 216, 537 F.2d 393. Indeed, in the months leading to the termination, the contractors were spending $120-150 million of their own money every month. *McDonnell Douglas XIII*, 76 Fed. Cl. at 427. Captain Lawrence Elberfeld, the Navy's A-12 Program Manager, testified that the cost to complete the A-12 contract would be so "unthinkably" over the fixed-price ceiling that the contractors' internal "worst case estimate could bankrupt both corporations." *Id.* at 429.

More importantly, Captain Elberfeld testified that the cost overruns jeopardized the contractors' performance because the contractor engaged in "cost

cutting efforts like reducing staff, eliminating overtime, quick fixes that address and would remedy a cash flow situation." *Id.* at 428. For example, around the time when the contractors missed the original first flight date, they removed 110 people from the A-12 program. *Id.* Captain Elberfeld concluded that the contractors' cost cutting efforts to avoid bankruptcy led to "more corner-cutting and more incomplete effort and basically a longer process to get a product that may not be the product that we desire or need for the Navy." *Id.* at 429.

c. Conclusion

In summary, the government offered the contracting officer's testimony, the contractors' statements, and contemporary documents as direct evidence. The evidence, such as the contractors' performance history (e.g., the failure to meet several milestones, including the significant first flight), coupled with the contractors' dire financial difficulty, which negatively impacted their performance under the contract, shows that the contracting officer was reasonably justified in feeling insecure about the contractors' rate of progress. Therefore, the government has satisfied its burden to justify the default termination.[4]

[4] Our current analysis may appear different from the one we previously instructed the trial court to perform, specifically, to determine the contract completion date. *See McDonnell Douglas XII*, 323 F.3d at 1018. We believe that this is warranted as under the law of the case doctrine, "it is not improper for a court to depart from a prior holding if convinced that it is clearly erroneous and would work a manifest injustice."

Once the government has met this burden of proving that timely performance is beyond the contractors' reach, the contractors have the burden of going forward to prove either that they were making progress such that timely completion of the contract was not endangered or that there was excusable delay. *See Appeal of Mich. Joint Sealing, Inc.*, ASBCA No. 41477, 93-3 BCA 26,011 (Apr. 26, 1993). On appeal, the contractors assert no affirmative defense. They proffer no record evidence to show, without contract restructuring, that they could have completed the contract on any date. Certain arguments, such as waiver, are presented to support their proposition that, at termination, the A-12 contract lacked an enforceable completion date. Even if these arguments could be interpreted as the contractors' defenses, we have already addressed them elsewhere in this opinion. In conclusion, because the government was justifiably insecure about the contract's timely completion and the contractors do not argue that their failure to make progress could be excused, we sustain the default termination of the A-12 contract.

3. Default termination without contracting officer's Lisbon analysis

The contractors and the *amicus curiae* also assert that we cannot uphold the default termination because the contracting officer, Admiral Morris, did not conduct the *Lisbon* analysis before the termination. They base this argument on the trial

Arizona v. California, 460 U.S. 605, 619, 103 S. Ct. 1382, 75 L. Ed. 2d 318 (U.S.1983).

court's finding that "Admiral Morris did not determine the entire effort required and the time left to complete that contract effort prior to termination." *McDonnell Douglas XIII*, 76 Fed. Cl. at 424 n. 72; *see also id.* at 437 n. 92 (concluding "the contracting officer did not conduct a *Lisbon* analysis prior to termination"). This argument is unpersuasive.

First of all, as we have stated earlier, because the modified A-12 contract does not contain a fixed completion date, a *Lisbon* analysis cannot be strictly applied. Second, we previously stated that "the government is not required to establish that the contracting officer conducted the analysis necessary to sustain a default under the alternative theory." *Empire Energy Mgmt. Sys. v. Roche*, 362 F.3d 1343, 1357 (Fed. Cir. 2004); *see also Christopher Vill., L.P. v. United States*, 360 F.3d 1319, 1337 (Fed. Cir. 2004) ("This court sustains a default termination if justified by circumstances at the time of termination, regardless of whether the Government originally removed the contractor for another reason." (quoting *Kelso v. Kirk Bros. Mech. Contractors, Inc.*, 16 F.3d 1173, 1175 (Fed. Cir. 1994))).

The contractors and the *amicus curiae* attempt to distinguish the present case from *Empire Energy*. The *amicus curiae* emphasizes that there is a "critical distinction between failure to make progress as the asserted basis for default at the time of termination, and failure to make progress as an alternative basis for default, proven at trial, that supports an otherwise unsustainable termination for failure to timely deliver." We discern no such distinction. In fact, the *amicus*'s contention is

illogical-it would have us, on the one hand, uphold a default termination for failure to make progress when the contracting officer never even contemplated, much less evaluated, such a basis; while at the same time, reject another default termination for failure to make progress even though the contracting officer explicitly asserted such a basis.

More importantly, we are less concerned about the label of the contracting officer's action so long as, in fulfilling his duty, the contracting officer exercised reasoned judgment and did not act arbitrarily. After reviewing the record, we believe that the contractors are not victims of arbitrary government action. Admiral Morris testified that concerns about the A-12 Program "increased [and] the risks increased" in the fall of 1990. *Id.* at 424 n.70. The trial court found that

> [a]s the end of 1990 approached, [Admiral Morris] was concerned that substantial development on the aircraft had yet to occur. He testified "[t]he contractors were indicating that they were experiencing an overrun that they could not absorb. Cost was obviously a factor and their failure to fabricate components, their failure to meet schedule were clearly impacting cost."

Id. at 423-24.

Admiral Morris also testified that in the weeks leading to termination, the contractors "indicated that they would not be able to meet the delivery schedule that was currently in the contract. And

they would not be able to perform the contract without extraordinary relief or additional funding for the contract." *Id.* at 424 (alterations omitted). He explained: "I didn't know at that particular time when in fact they would be able, if ever, to achieve performance of the contract and I was hearing 'we will not' or 'we could not.' " *Id.* (alterations omitted).

On December 17, 1990, Admiral Morris issued a cure notice, warning the contractors that their performance was "unsatisfactory" and the defect conditions were "endangering performance" of the contract. He explained that "[t]he purpose of the cure notice was to advise the contractors they were failing to make progress." *McDonnell Douglas XIII,* 76 Fed. Cl. at 402. He testified that he "had been extremely concerned with the communications coming in from the contractors that unless extraordinary relief were provided, unless the contract were restructured into a cost-type contract, that they could not or would not perform, and that belief existed certainly on December 17th."

Admiral Morris considered the problems of cost overruns to be a "real issue." *McDonnell Douglas XIII,* 76 Fed. Cl. at 404. Even though he made an effort to resolve the issue "within the context of the contract" without restructuring the contract, "the contractors were insisting upon Public Law 85-804 extraordinary relief."[5] Even in their January 2, 1991,

[5] Pub. L. No. 85-804, 72 Stat. 972 (1958) (codified as 50 U.S.C. § 1431), authorizes the President of the United States to grant agencies the power to provide extraordinary relief in furtherance of national defense.

written response to the cure notice, the contractors again requested restructuring the contract to a cost reimbursement contract. On Sunday, January 6, 1991, Acting Under Secretary of Defense Donald Yockey told Admiral Morris that Secretary Cheney would not provide 85-804 relief. As a result, Admiral Morris thought that

> he had three choices: to terminate the contract for convenience, to terminate the contract for default, or to do nothing. He rejected the latter as 'irresponsible,' thus focusing his attention on the other two choices. He eliminated the termination for convenience first, because he believed Contractors to be in material breach of the contract.

McDonnell Douglas X, 182 F.3d at 1328.

Record evidence shows that at the time of termination, Admiral Morris was justifiably insecure about the contract's timely completion. In addition, "a court's review of a default justification does not turn on the contracting officer's subjective beliefs, but rather requires an objective inquiry." *McDonnell Douglas XII*, 323 F.3d at 1016. In this regard, the facts in the record are sufficient for the court, in a de novo review, to sustain the default termination. *See Joseph Morton Co. v. United States*, 757 F.2d 1273, 1277 (Fed. Cir. 1985) ("It is settled law that a party can justify a termination if there existed at the time an adequate cause, even if then unknown.").

4. Conclusion

This is indeed an unfortunate case for all the parties involved. We realize that the court is not in a position to question the wisdom of the parties in entering this contract and subsequently, in handling problems in this case. Nevertheless, as the trial court recognized, "the Government rarely terminates fixed-price research and development contracts for default." *McDonnell Douglas XIII*, 76 Fed. Cl. at 418. We also observe that the CEOs of both MDC and GD, in a letter dated June 27, 1990, stated that "it was a mistake for the U.S. Navy to stipulate this type of contract and it was a mistake for the contractors to accept it. Both are at fault." Alas, the law of contracts does not allow us to deviate from established principles of law and equity. We therefore hold that the default termination of the A-12 contract is justified.[6] However, we emphasize that terminating a government contract for failure to make progress when the contract does not specify a completion date is the exception, not the norm. Therefore, we reiterate that the *Lisbon* test remains good law and our conclusion here is dictated by the unique facts of this case.

IV. CONCLUSION

For these reasons, the judgment of the Court of Federal Claims is affirmed.

[6] The government argues that the contractors' failed to provide adequate assurance. As we hold that the default termination for failure to make progress is justified, we do not need to reach this argument.

COSTS

Each party shall bear its own costs.

AFFIRMED

APPENDIX B

United States Court of Federal Claims.

McDONNELL DOUGLAS CORPORATION
and General Dynamics Corporation,
Plaintiffs,

v.

UNITED STATES of America,
Defendant.

No. 91-1204C.
May 3, 2007.

ORDER AND OPINION

HODGES, Judge.

The United States contracted with McDonnell Douglas and General Dynamics to design and build stealth aircraft for the Navy, then abruptly terminated the contractors for default. The contractors sued to convert the default to termination for convenience of the Government. The A-12 contract was technically complex, as might be expected of a major new weapons system, and the parties anticipated many years of development. The projected cost exceeded $4 billion in the initial stages. The purpose of the Full-Scale Engineering and Development (or FSED) contract was to design, develop, manufacture, and test eight A-12 aircraft. The eighth plane would serve as a prototype for subsequent production aircraft. Upon successful completion of the FSED effort, the Government could direct plaintiffs to begin a production phase. A series of options authorized the A-12 production phase in the contract by which the

Government could purchase production "Lots" of aircraft. At termination, the Navy had exercised its contractual right to order six production aircraft, known as Lot I.

Almost from the beginning, the contractors encountered problems that caused them to fall behind schedule. McDonnell Douglas and General Dynamics were to deliver the first test aircraft in June 1990. It became apparent well before then that the contractors would not meet that schedule. The first test aircraft was a key milestone in development of the A-12 known as first flight. The parties were unable to agree on rescheduling first flight and the succeeding seven aircraft of the FSED phase. The Navy extended the delivery dates unilaterally to accommodate the delayed prototypes. This unilateral modification of the contract's schedule was designated P00046. P00046 lies at the heart of this dispute.

The issue on remand is "whether the Government's default termination was justified." *McDonnell Douglas Corp. v. United States,* 323 F.3d 1006, 1014 (Fed. Cir. 2003). *FAR* 52.249-9 describes the Government's authority to terminate a research and development contract for default. That section authorizes the Government to terminate a contract if the contractor fails to "prosecute the work so as to endanger performance of th[e] contract." *FAR* 52.249-9(a)(1)(ii).

We review defendant's default termination according to the " *Lisbon* standard." *McDonnell Douglas,* 323 F.3d at 1015; *see Lisbon Contractors, Inc. v. United States,* 828 F.2d 759 (Fed. Cir. 1987). The

Lisbon standard permits termination for default if the Government demonstrates that the contracting officer had a reasonable belief " 'that there was no reasonable likelihood that the contractor[s] could perform the entire contract effort within the time remaining for contract performance.' " *McDonnell Douglas,* 323 F.3d at 1016 (quoting *Lisbon,* 828 F.2d at 765). The Court of Appeals for the Federal Circuit emphasized the importance of "decid[ing] the actual performance that the contract requires and the amount of time remaining for performance" before making that determination. *Id.* at 1017 (citing *Lisbon,* 828 F.2d at 766). In fact, the Circuit observed:

> Unless the contracting officer had determined the entire effort required under the contract and the time left to complete the contract, it would be difficult, if not impossible, for him to resolve whether there was no reasonable likelihood that the contractor could perform the *entire contract effort within the time remaining for contract performance.*

Id. (internal quotation marks and citation omitted). The parties disagree about the meaning of the Circuit's remand directing the court to apply the *Lisbon* test in this research and development contract.

The contractors urge the court to employ a strict interpretation of the Circuit's remand. That is, "the entire contract effort" must be all-inclusive, comprising the eight FSED aircraft, the six Lot I production aircraft and years of follow-on testing, aircraft main-

tenance, and contractor support for the Navy. Plaintiff McDonnell Douglas argues that no contracting officer could reasonably have terminated the A-12 contract for default for failure to make progress if he did not know the work left to be done and the time left to do it.

The Government offers a more flexible approach. The "entire contract effort" as used by the Circuit represents a convenient and enforceable yardstick this court can use to evaluate the contractors' progress at termination. Time was of the essence in the A-12 contract, and plaintiffs had an obligation to make enough progress to insure performance was not endangered. This court should decide whether the weight of the evidence in the record shows that the contracting officer was reasonably justified in feeling insecure about the contract's timely completion.

Defendant's argument is important in that the size of the yardstick does not matter. That is, the "entire contract effort" need not include every segment of work envisaged by the contract, but may be any objective measure of the contractors' progress at termination. Defendant's suggestion that we use a reasonable yardstick to measure performance is attractive for its flexibility and its simplicity, but it may be foreclosed by earlier rulings of the Federal Circuit.

The A-12 contract did not define "the time remaining for contract performance," as plaintiffs have interpreted that phrase. The contract has no "time remaining for contract performance" as in supply, service, and construction contracts. Defendant can-

not prevail if the law requires an enforceable contract completion date at termination. That is, if the date we must look to in measuring the contractors' progress can occur no earlier than after completion of plaintiffs' contract requirements, we would vacate the termination for default. *See Divecon Servs., LP v. Dep't of Commerce,* GSBCA No. 15997, 04-2 BCA ¶ 32,656, 2004 WL 1405648 (June 22, 2004) ("Without a ... specific completion date, the Government could not rationally terminate for default for failure to make progress, since there was no objective against which the contractor's progress could be judged."). The contracting officer did not know in January 1991 when contract completion might occur.

Defendant's burden of proof does not necessarily require the Government to provide a completion date for the entire contract effort, however. The FAR default provision does not refer to contract completion. The Circuit emphasized the importance of that requirement repeatedly, but the court also suggested other factors for consideration. Comparison of the percentage of work completed with the time remaining is only one consideration. *McDonnell Douglas,* 323 F.3d at 1016-17. The time remaining for performance is part of the "objective inquiry" under *Lisbon. Id.* Defendant's inability to establish a completion date for the A-12 contract does not compel a ruling for plaintiffs.

The ruling in this case depends on a discrete element of contract performance used as a yardstick to measure the contractors' progress at termination. The Navy's unilateral modification known as P00046 serves this purpose. The schedule for P00046 con-

tained benchmarks for performance and enforceable delivery dates when termination occurred in January 1991; it represents the "entire contract effort" the Circuit requires for measuring performance. This yardstick enables the court to consider the contractors' progress in light of factors that are probative of their ability and willingness to perform.

This Opinion also discusses "other factors usually relied on by courts and contract boards," for determining contractors' progress. *Id.* The contracting officer could have concluded that McDonnell Douglas and General Dynamics had "no reasonable likelihood" of delivering the aircraft on time as measured by the P00046 schedule. We must again uphold the Government's default termination of the A-12 contract.

I. BACKGROUND

The Government began development of the A-12 Avenger in 1984. The agreement between the Navy and the contracting team of McDonnell Douglas and General Dynamics was an incrementally-funded, fixed-price full-scale engineering and development (FSED) contract. Its purpose was to design, manufacture, and test eight A-12 prototypes. The Navy would use the prototypes to test various aspects of the aircraft's design; it maintained options to order production aircraft later.

The contract schedule required plaintiffs to deliver the first prototype in June 1990. Seven additional prototypes were due monthly through January 1991. The Navy exercised its option to purchase Lot I of the production models in May 1990, before the

contractors were to deliver the first prototype. As it became clear the contractors would not make first flight in June 1990, the Navy issued a unilateral contract modification in August 1990, extending first flight to December 1991. Known as P00046, the modification extended the seven additional A-12 prototypes through February 1993.

The United States terminated plaintiffs' contract for default in January 1991, nearly a year before the first flight was due.

A. THE A-12 CONTRACT

Plaintiffs' incentive contract had a target price of approximately $4.38 billion, and a ceiling price of $4.77 billion. The Government would pay forty percent of any costs over the contract price and below the ceiling price. The contractors would pay the remaining sixty percent, and all costs over the ceiling price.

The contract required the Navy to make payments in eleven installments from the date the parties signed the contract to the last payment on November 1, 1992. The terms of the installment payments were contained in Clause H-7 of the contract, which stated,

> (a) This financing arrangement is necessitated by the unavailability for obligation, at the outset of this contract, of sufficient funds to cover the total target values or ceiling price of the basic FSED contract line items.

(b) The Contractor agrees that the Government's obligation of funds in the amounts and by the dates set forth below will permit compliance with the contract. The Contractor acknowledges that the terms and conditions of the performance of this contract have been established on the basis that the Contractor's termination liability will not exceed the amount set forth below by the dates set forth opposite said amounts. Nothing herein shall authorize nor require the contractor to incur costs, plus a reasonable allowance of profit, in excess of the total amount obligated at any given time....

(c) In the event the Government fails to obligate any specified installment by the time specified, the Contractor [ ]will continue performance of the contract only to the extent that he shall not be required to incur obligations (termination liability) beyond that amount already obligated by the Government.... The Government's total obligation for payment (including termination settlement expenses) under this contract shall not exceed the total amount obligated at the time of termination.

...

(e) Nothing contained in this clause shall affect the right of the Government to terminate this contract pursuant to either

the "Default" or "Termination for Convenience of the Government" clauses.

The A-12 Program encompassed contract phases such as Concept Formulation, Full-Scale Development, Demonstration/Validation, and Full Rate Production. The Navy obtained approval from the Defense Acquisition Board, or DAB, at each development phase. The Navy agreed to proceed with Full-Scale Development (FSED) after the Defense Acquisition Board approved the Demonstration/Validation phase in January 1988.

The contract required plaintiffs to design, build, and test eight A-12 prototypes, manage the work according to the contract schedule, and provide logistical support to the Navy.[1] Section B of the contract consisted of a series of Contract Line Item Numbers, or CLINs. Each was tied to a particular aspect of work. For example, CLIN 0001 was the ATA Aircraft Initial Design Review (IDR). The contract contained fifty-six CLINs, numbered 0001 through 0058, at a total cost of $4,379,219,436. Lot I production CLINs ranged from 0101 through 0133. Four CLINs were deleted eventually from the contract's requirements.[2]

[1] The Navy's solicitation stated: "The intent of the Navy is to procure under one contract, the design, fabrication, test, and evaluation efforts necessary to qualify the ATA Full Scale Development (FSED) aircraft for production."

[2] The Navy could have moved to the Full Rate Production phase if the contractors had built the eight prototypes. Therefore, Section B of the A-12 contract contained CLINs for the production options of the contract. Option Item 0101 was the six production aircraft in Production Option I, or Lot I. Lot I accounted for thirty-one additional CLINs. Option Item 0201 corresponded to

Section C of the A-12 contract contained the Work Statement. The CLINs in section C were divided among five areas of performance: design, manufacturing, testing, support, and management.

1. Design

The design phase called for a series of performance reviews to ensure that the A-12 design was progressing according to contract requirements. CLIN 0001 was Initial Design Review. This review assessed whether "the selected aircraft design approach [wa]s compatible with the engineering requirements of the contract." It was "a means of determining that the contractor[s] ha[d] correctly understood all aircraft design and test requirements."

CLIN 0002 was the Preliminary Design Review, which "evaluate[d] the progress, technical adequacy, and risk allocation (on technical, cost, and schedule bases) of the selected design approach and determine[d] its compatibility with performance and engineering requirements of the development specification." The contract stated that "completion and approval ... of the final [Preliminary Design Review] w[ould] result in authorization for the contractor [s] to proceed with the design of the [aircraft]."

CLIN 0003 was Critical Design Review (CDR). CDR would occur "when detail design and analysis [wa]s essentially complete (90%)." This review sought to examine "the potential of the detailed de-

eight production aircraft authorized by Production Option II, which contained thirty-two CLINs. Similar procedures applied to Options through Lot VI.

sign of the [aircraft] to satisfy the performance and engineering requirements of the [aircraft's] development specifications." Review at this level would take place over a number of sessions "consistent with the completion schedule for the individual design efforts." CLIN 0004 added, "[a]t the conclusion of the incremental CDRs a final CDR of approximately four working days will be held to summarize the results of the individual CDRs." The review program would be closed upon approval by the Navy of the final CDR. This would "result in authorization for the Contractor[s] to proceed with the design of the ATA aircraft." After approval of the design, the contractors would move on to manufacture.

2. Manufacturing

The contractors began the process of manufacturing the first prototypes after the Navy approved their design. The contract called for the "manufacture and furnish[ing of] eight (8) aircraft and associated mockups, models, and test articles in accordance with the Detail Specification for ATA Weapon System, SD-574-1."[3] Plaintiffs would develop Avionics Integration Laboratories "as needed to provide a technically acceptable product within schedule."

The eight FSED prototypes would undergo careful ground and flight testing of nearly every aspect of the A-12's design. Each test aircraft would be more complex than the last. The ground testing require-

[3] SD-574-1 is the "detailed Specification for Carrier Based Advanced Tactical Aircraft Weapon System." It outlines the A-12's technical specifications, which are contained in Attachments 2-11 in Section J of the contract.

ments were set forth in an addendum to the contract, attachments 12-18. These were the "Contract Engineering and Test Requirements for the Advanced Tactical Aircraft Weapon System." Flight testing would evaluate the aircraft's propulsion systems and its ability to take off and land from carriers at sea. These and other technical aspects, would be monitored from first flight through completion of TECHEVAL. Attachments 18-22 of the contract contain detailed descriptions of these flight tests.

The testing phase was sequential, in that later tests were dependent upon successful completion of earlier testing efforts. Rigorous testing procedures did not end with the eight prototypes. Production aircraft produced in Lot I would be used to test various aspects of the plane's performance as well.

CLINs 0051 through 0056 were tied to Phases I through VI of the contractors' testing responsibilities. Testing Phase VI overlapped with TECHEVAL,[4] the Navy's formal testing and evaluation program for the A-12. The purpose of TECHEVAL was to assure that the aircraft met technical requirements of the contract.

3. Testing

The A-12 contract provided that the Navy would monitor the contractors' progress during all phases of contract performance. CLIN 0005 stated that satisfactory completion of interim requirements would not

[4] CLIN 0056 required the contractors to "conduct Phase VI of testing ... as required to the completion of TECHEVAL on all TECHEVAL aircraft."

occur until the Government approved the results of tests, inspections, or analyses of such requirements. This line item established joint Navy-contractor aircraft conferences and reviews. These conferences included the First Flight Readiness Review and the Production Readiness Review. Contract line items related to maintenance, support, and management programs were 0021, 0024, 0035, 0037, and 0049.[5]

The most important requirement of the contract for our purposes is schedule. Schedule is the reason the contracting officer gave for default terminating the contractors; it is the remaining basis for evaluating the contractors performance.

4. Schedule

The delivery schedules are in Section F of the A-12 contract. Performance deadlines could be derived either from the Master Program Schedule, by referring to other CLINs in the contract, or from assigned

[5] Section E of the A-12 contract dealt with inspection and acceptance of the work by the Navy. With respect to FSED requirements, the contract stated,

> Initial Design Review (IDR) under Item 0001, Preliminary Design Review (PDR) under Item 0002 and Critical Design Review (CDR) under Item 0003 are not complete until these reviews on the entire aircraft have been completed and approved by NAVAIR (AIR-05), all action items have been closed (defined, with mutually acceptable resolution plans which specify a schedule and the party who has the action), and under CDR (Item 0003) the Lot IV proposal in accordance with clause H-22 has been received. Provisional acceptance of the first aircraft under Item 0005 will evidence completion of Item 0006....

calendar dates. For example, the final FSED aircraft was due initially in January 1991, an assigned date. Derived dates included Item 0001, Initial Design Review, due "[n]ot later than 6 months after contract award." Item 0002, Preliminary Design Review was due "[n]ot later than 12 months after Contract Award." Item 003, Critical Design Review, would occur "18 Months after Contract Award." [6]

The eight FSED aircraft provided for in Line Item 0005 were to be delivered on a schedule of approximately one per month beginning in June 1990. The final FSED aircraft would be delivered in January 1991, according to the original schedule. The FSED contract schedule originated from CLIN 0011, which stated,

> [t]he Contractor shall establish and maintain management activities in accordance with the Project Management Requirements for the ATA Aircraft Weapon system to satisfactorily complete the tasks required by this contract. The program management effort shall be established with authority delegated at appropriate

[6] The Navy awarded the A-12 contract on January 13, 1988. Tying the dates in Section F to the award date meant IDR would take place no later than June 13, 1988; PDR was due by January 13, 1989, and CDR would begin June 13, 1989. Section F stated that "Critical Design Review (CDR) is not complete until CDR on the entire aircraft has been completed, all action items have been closed (defined with mutually acceptable resolution plans which specify a schedule and the party who has the action), and the Lot IV proposal in accordance with clause H-22 has been received."

> levels. Individual assignments within the management organization shall facilitate single-points-of-contact for interface with Government Managers in a timely manner. The Contractor shall commit such resources as are necessary to accomplish the requirements stated herein. Program Management shall be accomplished in accordance with Attachment 24, the Program Management Requirements of the ATA Aircraft Weapon System, ... and Attachment 25.

The A-12 contract required plaintiffs to prepare a Master Schedule to "include all critical activities necessary to complete the work required by the contract" and the important Navy milestones defined in Attachment 25. Upon approval by the Government, the Master Program Schedule would be the "baseline schedule against which progress will be measured." Plaintiffs provided the Master Program Schedule in their Best and Final Offer, and updated the Master Schedule periodically. Their last update prior to contract termination was August 20, 1990.[7]

[7] Attachment 24 to the Contract included the following:

> 2.2 *Master Program Schedule.* The Contractor shall prepare a Master Schedule for the ATA Project. This schedule shall include all critical activities necessary to complete the work required by the contract. Critical paths shall be highlighted and sensitivity to changes in schedule or resource availability identified. Required government activities shall be included in the schedule, and any critical actions identified. Following joint Program Office and Contractor review and concurrence,

5. Other Contract Provisions

The A-12 contract contained clauses from Federal Acquisition Regulations that routinely appear in fixed-price contracts such as this. The following provisions were incorporated by reference from FAR and applied to the FSED contract, CLINs 0001 to 0058:

FAR 52.232-2	Payments (Fixed-Price Research and Development);
FAR 52.232-16	Progress Payments;

this schedule shall become the Master Program Schedule, and will become the baseline schedule against which project progress will be measured.

Attachment 25 identified the following critical milestones:

Milestone	Date
FSED Start	December 1987
First Flight	June 1990
TECHEVAL	April 1993
OPEVAL	June 1993-November 1993
BIS Trial	June 1994
O Level	July 1994
IOC	July 1994
Support	March 1996

FAR 52.232-17	Interest;
FAR 52.243-1	Changes-Fixed-Price;
FAR 52.249-2	Termination for Convenience of the Government; and
FAR 52.249-9	Default (Fixed-Price Research and Development).

Standard provisions for the production options were separate from the FSED portion of the contract. Most were the same, but the termination clause was an important exception. The contract for production lots incorporated FAR default provisions for Fixed-Price Supply and Service contracts.

The parties agree that plaintiffs were to design, construct, and test the A-12, support the Navy in its tests of the aircraft, and manage work according to the contract schedule. They were to perform the work in a sequential fashion, so the projects would build on each other. The design phase came first, followed by production, then testing. The parties disagree about practically everything else.[8]

The Naval Air Command, referred to as NAVAIR, awarded the A-12 contract to General Dynamics and McDonnell Douglas on January 13, 1988. The contractors began work immediately.

[8] The appeals court made reference to reopening the record, leaving that matter to the trial court's discretion. The parties agree that this court has all the information necessary to rule on the issues at hand. *See infra* note 54.

B. CONTRACTORS' PERFORMANCE

Performance of the FSED contract on schedule was more difficult than expected for a number of reasons. No one had developed a stealth fighter with the A-12's flight capabilities. The science and technology required was state-of-the-art. The United States Air Force chose not to share its highly sensitive stealth information sufficiently to avoid technical difficulties and delay. [9]The Air Force eventually made much of the needed information available but it was too late in the process, according to the contractors. The plaintiffs' progress in key areas of performance prior to termination are summarized in the following sections.

1. Design

The Navy conducted design reviews to assess plaintiffs' progress on the A-12 design. Critical Design Review was among the last steps in this process. Admiral John Lockard was responsible for overseeing the design reviews. He testified that Critical De-

[9] Compartmented "state secrets" normally belong to and are controlled by government agencies rather than "the Government." Rules for handling so-called Black Programs vary among the agencies. This tends to cause friction in this case, between the Navy and the Air Force. As one example, the agencies' rules defining "need to know" are entirely different. The contractors wanted and needed highly sensitive technical information for the A-12, and the Navy wanted them to have it. This created many legal and logistical problems unrelated to the merits, and required substantial and frequent court involvement. Security personnel assigned to this court, our office of the Clerk of Court, and professionals attached to the Department of Justice, provided advice and assistance.

sign Review would "provide a sense of [whether] the requirement [would] be satisfied by the product in its detailed design state, [then] ensure that the product is producible; in other words, that [the contractors] could build them in a repetitive way such that ... one airplane looks like the next airplane."

The CDR process offered the Navy an opportunity to raise lingering concerns about technical progress through Requests for Action, or RFAs. The Navy made 433 such requests. By the close of CDR, Admiral Lockard had signed all 433 Requests for Action. Admiral Lockard stated at trial that "[e]ach [RFA] had been signed by me, indicating that as far as I was concerned, I had reached agreement with the contractor." His signature provided evidence that the parties had resolved issues represented by Requests for Action.

Admiral Lockard closed the formal Design Review Board activity on October 22, 1990, and stated "[a] fair agreement has been reached, one which will provide the Navy with the product they need." He added, "[t]echnical resolution on the airplane" was accomplished as well. Admiral Lockard thought the Navy and the contractors were "in the process to a satisfactory conclusion of CDR." He wrote that the "product as defined [in the CDR activity] will meet [the Navy's] operational requirements."

At the same time, Admiral Lockard reported to Navy Secretary Gerald Cann a "lingering technical concern" on some design and production aspects. Admiral Lockard noted in particular that

> the tooling concept that was being used to build these very complex parts was one which there was much debate about. [C]ould that [concept] really produce [?] Until we could get some consistency, it was hard ... to make a determination that, in fact, they could do this repeatedly at a production rate sufficient to produce parts to support a production line of so many per month.[10]

During the Count XVII trial, Admiral Lockard described the contractors' difficulty in manufacturing the major structural components of the aircraft, termed "big bones." He explained that it was the first time anyone had built a structure of this size, with the materials being used. The "big bones" were

> critical to the design-to the integrity of the airplane, and [the contractors] were not making progress in building these. As a matter of fact, they were severely behind and going further behind in building these parts, and we couldn't assemble the first airplane until they were able to build these parts successfully.

[10] Admiral Lockard's message to Secretary Cann was intended to convey the Navy's "need[ ] to ensure that [it] worked with the contractor to improve their ability to get yield from the parts in a predictable way, and if we didn't do that, then [the Navy and the contractors] weren't ready for production." Asked why production would not occur on time, Admiral Lockard responded, "[b]ecause you couldn't predict how much the airplanes were going to cost if you didn't know how long it was going to take to get the number of parts required to build it."

These were concerns expressed about the Admiral's findings at CDR. As termination approached, Admiral Lockard testified about

> almost daily meetings between Admiral Morris and myself, trying to figure out how we were going to be able to resolve this and keep this program on track. So we discussed all of the technical issues, could we get them resolved, if we could find a way to satisfy the business arrangements, to get the contractors to do the work, and we were certain that we could do it. We were unsuccessful in my discussions, though, at that point of finding a way to get the contractors to do the work.

When asked his assessment of the contractors' ability to manufacture composite parts at termination, Admiral Lockard responded,

> there was still an awful lot of uncertainty in the ability, particularly for General Dynamics. The tooling concept that they had chosen, I was very concerned that it was going to be able to produce parts in a repeatable fashion. They had not been able to stabilize it. I thought it was critical in nature, and I was concerned that it was going to take us more time to work that tooling concept out in order to have one that could produce with certainty parts that could be used on a continuing basis.

However, Admiral Lockard closed the formal Defense Review Boards because the technical problems

had been resolved. He stated at adjournment that "[a] fair agreement has been reached, one which will provide the Navy with the product they need." The Admiral concluded, "technical resolution of the airplane has been reached."

The contractors worked on the Program during and after the design reviews. Technical agreements between plaintiffs and the Navy caused the contractors to modify their work in some cases, often changing the agreements from original contract requirements. Officials from General Dynamics and McDonnell Douglas understood that the contract work should continue according to the agreements reached at CDR. When CDR closed, the parties had negotiated a critical path toward completion of the design and development of the aircraft.

Mr. Lamers of General Dynamics made the following announcement at an "all hands meeting" in November 1990:

> The critical design review is completed, this is the end of the ... three major reviews that have been taking place over the last more than two years. Thirty-eight significant issues were resolved. We've closed 433 requests for action .... [a]nd it does constitute the Navy's formal approval [and] ratification of the design of the A-12.[11]

[11] The Government accepted plaintiffs' design just over a month before its decision to terminate plaintiffs for default for failure to make progress.

The Navy knew months prior to the final Critical Design Review that the A-12 would not meet some of the technical specifications in the contract. Despite such knowledge, the Navy agreed that technical concerns had been addressed and resolved to its satisfaction. The Navy accepted plaintiffs' design for the A-12 in November 1990.[12] The next issue was whether the contractors could manufacture the plane according to the designers' intent.

2. Manufacturing

The contract required plaintiffs to "design, develop, manufacture and furnish eight (8) Full Scale Engineering Development (FSED) aircraft and associated mockups, models, and test articles in accordance with the Detail Specification for [the Advanced Tactical Aircraft] Weapon System...." The contractors would employ a "building block" approach, building each succeeding prototype to be significantly more complex than the previous one. The first prototype

[12] The Government contends that the court may not use the agreements reached at CDR as waiver of nonconformance by the Government because such agreements were not signed formally. The contractors maintain that the parties considered themselves bound by the agreements at that time, despite the lack of formal signatures. The issue is not whether the agreements are legally binding documents in any event. The agreements provide additional evidence that the Government had accepted plaintiffs' design. Moreover, government officials commented at trial that these "handshake agreements" had the weight of contractual force, and everyone intended to honor them. The Navy's relationship with plaintiffs was a solid and impressive one throughout. They worked together closely and both sides handled day-to-day affairs of the relationship honorably.

would test the A-12's ability to fly. Once the Navy and the contractors knew the first aircraft would get off the ground, the contractors would address other capabilities of the plane in subsequent prototypes. For example, the second prototype would test the propulsion system. Other FSED aircraft would examine the A-12's avionics and carrier suitability. *See, e.g., McDonnell Douglas Corp. v. United States,* 35 Fed. Cl. 358, 362 (1996). ("Each FSED aircraft would test different characteristics of the A-12; stealth capabilities would be verified in the 'fully capable, fully equipped' eighth aircraft that would serve as the basis for the production lots.").

The companies monitored the A-12's manufacturing schedule carefully. Mr. A.L. Briggs was the Vice President of McDonnell Douglas for Manufacturing Operations. His December 12, 1990 report assessed the A-12's manufacturing performance, the study of which he began in March 1990.

Briggs' March investigation "revealed serious differences between the program status reports and the actual conditions on the shop floor and in the tooling and detail parts fabrication." While status reports were showing first flight in December 1990, his assessment was that first flight would be at least "four to six months later" than stated. He reassessed the program again in June and found "no improvement." In fact, he believed "the program had worsened somewhat." Such assessments were grim, but McDonnell Douglas received more favorable commentary:

> The Technology exists and McAir Manufacturing has the ability to build the A-12 aircraft as designed. Fabrication, Assembly and Tooling are all geared up and focused on the job at hand. By creating a realistic schedule and managing to that schedule, McAir Manufacturing can deliver the major assemblies to Tulsa in accordance with the revised plan.

The report on General Dynamics was ominous. Mr. Briggs said, "GD engineers designed an airplane that GD Manufacturing could not build." He explained, "[t]he complexity of the composite parts was far beyond manufacturing's available technology in tooling and part fabrication." If Admiral Morris had been aware of this evaluation, it would have given him reason to be concerned about timely completion.[13] By December, however, Briggs had concluded that the "[m]anufacturing team is capable of building the A-12 aircraft as it is now defined.... The revised schedule for getting the major assemblies to Tulsa and the activity at Tulsa are energetic, but achievable."

Mr. Briggs compiled a year-end appraisal of the A-12 schedule position in December 1990, discussing the progress of "McAir, GDFW, and Tulsa" in meet-

[13] It may not matter whether Admiral Morris knew about such reports. The Federal Circuit ruled that so long as the information was available to the Government, the court may consider it in reviewing the contracting officer's decision. *See, e.g., Empire Energy Mgmt. Sys., Inc. v. Roche*, 362 F.3d 1343, 1357 (Fed. Cir. 2004).

ing the contract's revised schedule.[14] He concluded that the "Tulsa effort ... [wa]s progressing on plan." In St. Louis, the forward fuselage was "[p]rogressing satisfactorily," as was the aft fuselage, despite delays resulting from the Navy's rejection of certain parts. Work on the R/H Outer Wing "suffered severe set backs due to recently identified engineering changes" but the delivery date for the parts was "still achievable."

The report also discussed General Dynamics' offload issues. The "[t]ooling and parts fabrication are progressing [but] [a]pproximately 20 critical parts are being tracked by the Navy as potential show stoppers." The center fuselage was "[p]rogressing satisfactorily" to meet delivery dates, and the L/H Outer Wing was experiencing the same problems as the right outer wing. The Inner Wing assembly, however, was "in worse condition" than when the delivery schedule was established. The report indicated that there was "[n]o known resolution at th[e] time."

The delivery date was August 1991. Briggs felt the date was still achievable, but he was "losing confidence." He detected a "serious deterioration of the wing condition in the last few days." Under existing conditions, General Dynamics "probably will not be able to build the Inner Wing assemblies on or near schedule." He identified possible solutions for the

[14] McAir, General Dynamics Fort Worth (or GDFW), and Tulsa are references to the contractors' manufacturing centers. McAir was a division of McDonnell Douglas located in St. Louis, Missouri.

situation, including integration of a joint assembly team.

Mr. Briggs concluded the report as follows:

> I believe the March 1992 First Flight date is still achievable, but only after significant changes which I intend to pursue immediately after the reorganization.[15] My confidence in the March 1992 flight date is reduced to approximately 50% based on current conditions.

Mr. Dave Cormany of General Dynamics highlighted manufacturing problems in an interoffice memorandum sent December 14, 1990. He expressed this dissatisfaction:

> In walking through and actually touching the two surviving [aircraft] parts this morning, I am convinced that if either makes it, it will not be near term. Therefore, we must assume that, as of today, we have NO coverage for ships 1-3 for this part.
>
> ...
>
> I was very, very dissatisfied with the lack of control we had in inspection/support areas I visited today. We either had people sitting around with no work in areas we are calling critical, or we had parts

[15] The phrase, "immediately after the reorganization" highlights the importance that both the Navy and the contractors placed on restructuring the contract.

languishing in areas they had no business being, with no drive to work them or move them. Both are unsatisfactory.

I believe we can produce one piece of any rib part number each eight to nine days, if we really want to. If we want an A-12 program, we had best want to do so with all our hearts. SOUND "BATTLE STATIONS"! We are in desperate trouble.

Mr. Cormany sent a second memorandum on December 28, 1990:

Perhaps there is some misunderstanding regarding the urgency on the subject LH rib for SWBS 3810. This rib started layup approximately 19 December. It is still not complete. Since 26 December, I have personally visited the part of each shift day during the holiday and have been told daily there are no problems and that the part should go to cure "next shift." It still sits exactly as it did on that date.

Folks, we have NO PARTS for any aircraft of this part number. We are in a program day-for day side until the part reaches stock. We are currently breaching the drop-dead commitment date for the program of 31 March 1992, due to this part. I just do not understand how we can let the program critical parts sit for days and days. I am now very concerned with total out time accumulation for the part, in light of its

> extended layup period, and the upcoming week-end and holiday.
>
> PLEASE get someone working on this job, and get it done! ...

Plaintiffs' own technicians were not happy with the manufacturing process. The Navy seemed at least acquiescent prior to Pentagon intervention in December 1990, if concerned about the pace.

3. Testing

Ground testing was underway in December; flight testing would have begun with first flight. The Government terminated the A-12 contract for default nearly a year before first flight. Admiral Lockard described his frustration in November 1990:

> [No one could] predict with accuracy when we were going to fly the plane until we had, in fact, successfully built the parts for the first one. Because we were having difficulty building those parts, I could not come to a determination of when we would actually-with some level of certainty-fly the first airplane.

Admiral Lockard had expressed this concern at a Design Review Briefing in November 1990. He added, "[b]usiness factors still cloud [the] technical picture."

4. Business Issues

Work on the A-12 contract progressed over budget during the early stages of contract performance. Ms. Eleanor Spector, Deputy Assistant Secretary of De-

fense for Procurement, testified that "the contractor was spending at a rate of 120 million to 150 million per month." Admiral Morris stated that the contractors' "rate of investment on a monthly basis" was around $150 million.

Ms. Spector[16] explained how financial problems could affect contract performance:

> [W]hat generally happens when a contractor has financial problems is it's unable to do work-arounds. It's unable to do new technical approaches that may be necessary to solve a problem. That's particularly true in these fixed price development contracts where the whole contract is for development, and you have to keep trying different things if the first thing doesn't work. So when you're having financial difficulties, it becomes difficult to do new design approaches, necessary fixes to problems that inevitably arise.

Plaintiffs asserted that performing to the specifications on a fixed-price contract was impossible.[17]

[16] Eleanor Spector's testimony was valuable. Documents produced in discovery showed that she had insight approaching prescience. For example, she opposed putting the A-12 out for bids on a fixed-price contract. She relented only with assurance that the Government would share its stealth technology with the contractors. Otherwise, she predicted, it cannot be done.

[17] Donald J. Yockey, Acting Under Secretary of Defense (Acquisition), apparently agreed. Prior to termination, he lamented, "[w]hy did we ever go out on a fixed price contract? We should have learned long ago that you can't develop complex systems to a fixed price."

They wanted to modify the contract terms due to impossibility of performance and nondisclosure of superior knowledge regarding stealth technology. Secretary of the Navy Lawrence Garrett asked plaintiffs' CEOs in a June 20 letter to provide detailed descriptions of the contractors' proposed options for proceeding with the A-12 Program. The contractors stated that the fundamental problem with the contract was its fixed-price structure. They proposed modifications but could not reach an agreement with the Navy.

Plaintiffs warned the Navy in September 1990 that insufficient funds were obligated to the FSED portion of the contract. They asked that funding be provided at a more rapid rate "to preclude the possibility that the contractors may have to stop work under the contract." The Navy refused this request on October 3, and a similar request by the contractors in November, but obligated a scheduled $185 million installment to the contract on November 1, 1990.

C. SCHEDULE

Schedule problems have been an issue of paramount importance in the history of this case. They caused the Government to waive the requirement for first flight in June 1990, creating a *DeVito* waiver issue that is crucial to plaintiffs' case. *See DeVito v. United States,* 188 Ct. Cl. 979, 413 F.2d 1147 (1969). Schedule problems caused the Navy to issue P00046, which overlapped the original contract schedule for Lot I and created a "nonsensical" situation. The P00046 schedule serves as the court's standard for measuring plaintiffs' performance.

The Federal Circuit ruled that the trial court should determine whether plaintiffs were in default at termination. We focused on schedule because other reasons that Admiral Morris gave for terminating the contract were not valid. *See McDonnell Douglas,* 323 F.3d at 1011; *McDonnell Douglas Corp. v. United States,* 50 Fed. Cl. 311, 319-24 (2001). Schedule again appears to be a key to resolving this case. The issue is whether the Government's termination for default is justifiable. Schedule is one basis for deciding reasonableness of the Government default decision. To know whether the termination was reasonable, we must know the amount of time remaining on the contract, according to the Federal Circuit. *McDonnell Douglas,* 323 F.3d at 1017.

1. First Flight

The A-12 contract included four options that permitted the Navy to order production aircraft delivered through 1995. The Lot I option was executed by the Navy on May 30, 1990, requiring plaintiffs to manufacture six A-12 production aircraft in addition to the FSED prototypes. This meant the contractors would deliver fourteen aircraft on dates certain through May 1992. The contract contained the following schedule for delivery of prototype and optional production aircraft:

Aircraft Number	Delivery Date
1	June 1990
2	July 1990
3	August 1990

	4	September 1990
FSED	5	October 1990
	6	November 1990
	7	December 1990
	8	January 1991
	9	June 1991
	10	August 1991
	11	October 1991
LOT I	12	December 1991
	13	March 1992
	14	May 1992

The contractors did not achieve first flight in June 1990. The Navy took no steps to terminate the contract.[18] However, the contracting officer at the time sent a letter to the contractors in July stating that they had not delivered the first aircraft in June as required by the contract and warned of the consequences of failure.[19] Negotiations for rescheduling the contract ensued.

[18] The Navy knew in Spring 1990 that the contract schedule would have to be restructured. Plaintiffs asked Captain Elberfeld, the Navy's A-12 Program Manager at the time, "[w]hen the first flight date was missed, what did you do about it?" He responded, "we all knew very well for many months before that it was not going to be achieved. I don't recall taking any specific action immediately after it passed."

[19] Contracting Officer Mutty sent a letter to the Team on July 12. He expressed "serious concern regarding [their] performance under the A-12 contract." They had "failed to deliver the first aircraft as required by the contract ... [and that] failure

The contractors' CEOs were John McDonnell and Stanley Pace. They presented a review of the A-12 Program to Navy officials on June 13, 1990. The major discussion points were Technical Issues, Schedule, and Cost Status. The report stated that weight of the aircraft was the top concern, but appeared to be "under control." The CEOs reported "No Major 'Showstoppers' " on technical issues. Schedule was next.

Management predicted first flight in the July 1992 through September 1992 period. The remainder of the FSED schedule would be twelve to fourteen months beyond the original plan. Cost estimates at completion were "still in work, [with] a large variance between estimates," according to the CEOs. They acknowledged that significant challenges remained, but announced that the Program was under control. They discussed conclusions and recommen-

could jeopardize performance of the entire FSED effort." He continued,

> [n]either your letter nor afterward have you provided any basis on which I could conclude that any of your obligations under the contract should be excused. The little information you have provided is far from adequate to permit an assessment of the state of your performance under the contract.

Mutty directed the contractors to inform the Navy when they would deliver first flight, their plan to meet the remaining FSED schedule, and their consideration for proposed contract modifications. He concluded with the following remarks: "[T]he Navy believes the contract is valid and enforceable on its terms. The Navy is not waiving any of its rights under the contract by affording you the opportunity to respond with detailed information."

dations at the high-level meeting, using slides with the following captions:

CONCLUSIONS

- System Performance is Good With Excellent Overall Operational Capability
- The Predicted Cost of the FSED Program Will Exceed the Ceiling by a Magnitude That the Companies Cannot Absorb
- The Production Lot Option Not to Exceed Prices Are Also Predicted to Exceed Those Specified in the Contract
- Current Schedule Does Not Match Contract Schedule
- Production Lot III Would Be Exercised Prior to Sufficient Testing to Demonstrate System Performance
- The Concurrence of the Program Will Likely Lead to Milestone IIIB Not Being Met

RECOMMENDATIONS

- The Program Teams, Government and Industry, Have Been Studying Various Approaches to a Restructured Program
- We Should Be Authorized to Complete this Study and Propose a Program and Business Arrangement That Is in the Best Interest of the A-12 Program, including:
  - -Deliveries Per Rephased Schedule for FSED and Lots 1, 2, 3 & 4
  - - Adjusted Specification

- Navy Added Requirements
- Contractor Claims

2. P00046

Mr. Lamers of General Dynamics was the principal program manager for the contractors. He predicted they could deliver first flight in July 1991. The Government undertook an assessment of whether this goal was obtainable. *See McDonnell Douglas,* 50 Fed. Cl. at 317 (noting "[t]he Navy wanted a reasonable schedule, not an unachievable one. The contractors and the Navy convened a strategy board to put together a realistic schedule for first flight."). The contractors were working to an aggressive schedule, but they would not sign up for one. They did not want to become contractually bound to a new schedule because of the uncertainties of controlling weight without having the benefit of shared technical information from the Air Force. Captain Elberfeld developed a plan to restructure the A-12 contract through the Defense Acquisition Board. He testified that the DAB would serve to

> get the program officially rebaselined. It would be the formal approval step necessary to get the program back into something that was manageable and controllable, in the sense of having the program documentation, the contract schedules, the financial and business arrangements and so on, all in place so that cost, schedule, and technical aspects of the program could be managed more efficiently, instead of working to a contract

> that had milestones that had already been missed ...

Elberfeld's plan included a "path to the A-12 DAB." He issued P00046 as a step along this path-a modified unilateral FSED delivery schedule for aircrafts one through eight.[20] According to Captain Elberfeld's plan, the parties would resolve the technical issues at CDR and the Navy would present the revised technical baseline to the DAB for a decision.

The Navy issued P00046 on August 17, 1990. The modification moved the due dates for the FSED prototypes back about eighteen months; the revised schedule called for first flight in December 1991. The modification spread the remaining prototypes out as well, doubling the time for delivery between each aircraft. Instead of one per month, P00046 required delivery of one prototype approximately every two months. Aircrafts two through eight were due February, June, August, September, November, and December 1992, and February 1993.

P00046 revised FSED aircraft delivery dates but left Lot I and later milestones intact. Captain Elberfeld testified that after he issued the contract schedule modification, the Navy had "no schedule for the

[20] Captain Elberfeld testified that he was the person responsible for issuing P00046 to replace the bilateral schedule in the original contract. He approached his duty in a methodical and conscientious manner, and his schedule was reasonable. *McDonnell Douglas,* 50 Fed. Cl. at 316-19. The Navy did not waive the new schedule by announcing other acceptable dates for first flight. *Id.* at 319. The Federal Circuit affirmed these 2001 conclusions. *McDonnell Douglas,* 323 F.3d at 1018-20.

Lot I aircraft that you would call a realistic schedule." This fact was generally accepted among Navy officials familiar with the Program. The contractors could not have delivered Lot I aircraft on the dates the parties originally intended because of an overlap.[21]

[21] The following chart shows that the schedule in place required plaintiffs to show that the first prototypes could fly before or at the same time they were to deliver fully-compliant production aircraft to the Navy:

Aircraft Number	Delivery Date	Aircraft Number	Delivery Date
ORIGINAL FSED		**P00046**	
1	June 1990		
2	July 1990		
3	August 1990		
4	September 1990		
5	October 1990		
6	November 1990		
7	December 1990		
8	January 1991		
LOT I			
9	June 1991		
10	August 1991		
11	October 1991		
12	December 1991	1	December 1991
13	March 1992	2	February 1992
14	May 1992	3	June 1992
		4	August 1992
		5	September 1992
		6	November 1992
		7	December 1992
		8	February 1993

Captain Elberfeld testified that the purpose of the unilateral modification was to serve as "a first step in achieving [the] overall delivery schedule...." The lack of new delivery schedules for Lot I "was not meant to imply that there was any intent or any thought that those aircraft could ... be delivered earlier than the FSED aircraft." [22]

The ultimate contract completion date sought by the remand order would be a moving target, if it exists at all. *See McDonnell Douglas,* 323 F.3d at 1017 (stating the Government must put forth " '*direct* evidence on the time which it estimated it would take [the contractor] to complete the contract' ") (quoting *Lisbon,* 828 F.2d at 766). In fact, if contract completion as envisioned by the Circuit should be a definite date by which plaintiffs were to complete entire contract performance, this contract did not provide such a date. Captain Elberfeld explained the expectations of performance with a research and development contract:

> The schedule for completing contracts is something that takes sometimes years. Some contracts ... [take] ten, fifteen years before they're closed out, even after the last

[22] Additional testimony from this witness confirms that it was "no one's idea to [deliver aircraft nine before aircraft one]." We had the impression during trial that the overlap was a clerical error or oversight. This enabled the ruling that the unilateral schedule was reasonable and therefore enforceable. *See McDonnell Douglas,* 50 Fed. Cl. at 318-19. It appears likely that the parties did not consider Lot I then; it was an oversight. They assumed the contract would be restructured before Lot I became an issue.

> aircraft is delivered.... I don't know what the schedule is to close out the contract. We had a schedule for delivering aircraft, we had a schedule for other milestones, like critical design review, preliminary design review, other major program milestones. But I don't recall the contract saying ... [it] will be completed and closed out on this date, as one of the requirements of the contract.

Captain Elberfeld's recollection was correct; the contract did not provide a close-out or completion date. Later he observed, with a research and development contract, "[u]ntil you get to the end, you don't know what the last step is."[23]

During the months leading to termination, the contractors' internal schedules were showing that first flight would not occur in December 1991. Their projections showed first flight delivery three months later, in March 1992. Navy officials testified that defendant could not predict when the contractors would deliver first flight.

[23] Captain Elberfeld was asked what level of contractor performance signified completion of the contract; i.e., what was the final act. Captain Elberfeld responded, "[i]t depended on what they were doing and what they were having problems accomplishing.... Until you get to the end, you don't know what the last step is." Captain Elberfeld testified that he had "certainly not" established a schedule for contract completion with modification P00046.

D. EVENTS LEADING TO TERMINATION

The Pentagon took over management of the A-12 Program in December 1990. Decisions regarding when and how to issue the notice to cure and other notices required by FAR originated from OSD. This development, along with the Government's need to obligate over one-half billion dollars to the A-12 program in January, marked the beginning of the end for the aircraft and for the contractors and their employees.

1. Department of Defense

The Department of Defense initiated a Major Aircraft Review during 1990 to investigate pending weapons systems. Its purpose was to determine whether proposed new aircraft were needed in the post-Cold War environment. The A-12 Avenger fell under that review.

The Secretary of Defense visited the McDonnell Douglas plant in March 1990, as part of the government evaluation of national defense needs in response to changing world situations and reduced national security threats. He learned of concerns about the Program, but remained confident the Navy and the contractors could deliver the aircraft. He expressed confidence in the A-12 Program, and he assured Congress that the Navy's need for the aircraft persisted. The Navy would continue pursuit of its development.

The Defense Secretary reported results of the Major Aircraft Review to Congress in April 1990.[24] His comments about the A-12 Program were reassuring. Secretary Cheney told the Committee that the A-12 was "one of our most urgent requirements." He testified about the Navy's need for the Program and its smooth course of development.

Weeks after testifying to Congress, the Secretary became aware of problems containing costs in the Program and maintaining the schedule. He was troubled because his report only weeks earlier had not reflected these concerns. He had testified in glowing terms about the aircraft and the contributions that it would make to the Fleet. The Defense Secretary was embarrassed and annoyed that he had to return with a different assessment for the Committee so soon. He had to report that the Program was seriously behind schedule and the projected cost of completion exceeded earlier estimates. The Secretary met with the contractors during the Summer of 1990 to address his concerns. He reiterated to the contractors his belief that the A-12 was a high-priority Navy program, however.

[24] The Secretary of Defense discussed the Major Aircraft Review before the House Armed Services Committee on April 26, 1990. He faced mounting concerns about the federal budget deficit, however, and congressional demands for military budget reductions. He recommended continued funding for the A-12, but at reduced levels. The planned purchase of 858 aircraft with a maximum production rate of forty-eight per year would be reduced to 620 aircraft with a maximum production rate of thirty-six per year. This had a significant impact on the per unit cost of the planes.

Two reports published in November 1990 had an impact on the A-12 Program. Both were critical of the Pentagon's part in the Major Aircraft Review. The Beach Report criticized the Navy's finding that the contract could be completed within its ceiling price, concluding that the program manager should have anticipated the extent of schedule risk. It criticized other Navy officials close to the Program as well. The other report, from the Department of Defense Inspector General, found that the Major Aircraft Review had not been conducted properly and otherwise was handled poorly.[25]

The Secretary of Defense signaled in December 1990 that he no longer supported continuation of the A-12 Program. He wrote a classified memorandum to

[25] The Secretary of Defense stated during his pre-trial deposition, "[t]he [Inspector General] has generally done good work for the Department of Defense. I don't always agree with them, but sometimes they produce good results. In this particular case, they recommended termination for default, which is what I ultimately did."

DOD counsel advised that the quoted excerpt from the deposition should read, "[i]n this particular case, *we* recommended termination for default which is what *we* ultimately did." (emphasis added). Government counsel presented the Secretary an errata sheet before trial. The Defense Secretary agreed that counsel's suggestions of error reflected more accurately what he believed occurred. If so, the decision presented by Admiral Morris on January 7, 1991 may have been removed yet another level, to the Inspector General's office. The Inspector General did not testify; his or her name did not arise during trial. The errata sheet was provided to plaintiffs' counsel and the court the morning of the Defense Secretary's trial testimony.

the President expressing his disappointment in the A-12 Program, the Navy's handling of production, and the Major Aircraft Review. He stated that he would take corrective action promptly. The Under Secretary of Defense for Acquisition resigned.

Citing "serious shortcomings" in the A-12 Program, the Secretary directed his Deputy to evaluate the A-12 and report back in ten days. OSD instructed the Navy to "show cause" by January 4, 1991, why the Defense Department should not cancel the Program. The show cause letter stated:

> The A-12 Program is in serious trouble. The apparent schedule slippage, cost growth, and management deficiencies in this Program are intolerable. If we cannot spend the taxpayers' money wisely, we will not spend it. Accordingly, I direct you to show cause by January 4, 1991 why the Department should not terminate the A-12 Program and pursue other alternatives.

Admiral Morris was the contracting officer then, but the Office of the Secretary of Defense had taken over management of the A-12 contract and the A-12 Program. OSD instructed the contracting officer to issue a notice to cure on December 17. Admiral Morris notified McDonnell Douglas and General Dynamics that the contractors' performance was "unsatisfactory." The cure notice to the contractors included the following warning:

> [T]he Government considers your performance ... unsatisfactory. Specifically, you have failed to fabricate parts sufficient

> to permit final assembly in time to meet the schedule for delivery of FSED aircraft. In addition, you will not deliver the Lot I pilot production aircraft in accordance with the contract schedule. Moreover, your failure to meet specification requirements, such as aircraft weight,[26] jeopardizes the carrier suitability of your design.

The contracting officer stated that such conditions were "endangering performance of [the] contract" and unless the problems were "cured by 2 January 1991 the Government may terminate for default" pursuant to FAR 52.249-9.

Admiral Morris explained his purpose in issuing the notice:

> The purpose of the cure notice was to advise the contractors they were failing to make progress, and that the Navy was extremely concerned that it would ... be able to get an aircraft that would satisfy its intended purpose in buying the aircraft. And so this was a means of asking the contractors to address the many issues that were being communicated to the contractors through various people through various means at the time, and to tell the Navy what it was going to do to address those issues.

[26] OSD's legal department directed the contracting officer to include weight of the aircraft as one of plaintiffs' deficiencies. This was incorrect. *See McDonnell Douglas,* 50 Fed. Cl. at 323; *McDonnell Douglas,* 35 Fed. Cl. at 373-74.

The notice to cure was an item on the checklist of requirements the Government must follow before terminating a contract for default. For all practical purposes, the decision to terminate had been made, but the notice created a sense of urgency among the parties. The notice also set off a series of high-level meetings among the principals.

2. Meetings Before Termination

Plaintiffs met with government officials on December 18, the day after the Navy issued the cure notice. The Government was represented by Donald J. Yockey, Acting Under Secretary of Defense (Acquisition), Terrence O'Donnell, General Counsel, DOD, Dennis Trosch, Associate General Counsel, DOD, Eleanor Spector, Deputy Assistant Secretary of Defense (Procurement), Gerald Cann, Assistant Secretary of the Navy (Research, Development & Acquisition), Craig King, General Counsel, Navy, and Rear Admiral William R. Morris, Assistant Commander for Contracts, NAVAIR, and contracting officer for the A-12.

The Contractors were represented by John McDonnell, CEO, McDonnell Douglas, and Jerry Johnston, President, McDonnell Douglas; and Bill Anders, CEO, General Dynamics, and Jim Mellor, President, General Dynamics. The purpose of the meeting was to discuss the contractors' response to the cure notice, and to decide whether perceived problems could be cured by January 2.

Mr. Anders conceded at the meeting that the aircraft was not on course. He said the A-12 would not fly in January 1991, and "[a]ll deficiencies cannot be

corrected." He said plaintiffs would "do the best we can, [to] deliver a satisfactory aircraft for the Navy, [but] Mother Nature won't allow correction of all defects." He left it to the Navy to decide whether the contractors' best was "good enough." He added, however, "[i]t's going to be a good airplane, one I would like to fly."

Under Secretary Yockey wanted to know whether the contractors would complete the FSED contract regardless of the cost; that is, "for whatever it takes." Mr. McDonnell's response was, [the contract] "has got to get reformed to a cost-type contract or we cannot do it. We need some form of Public Law 85-804." [27]

Admiral Morris took notes at the meetings that were held in response to the notice to cure. He offered interpretations of comments made at those meetings during his testimony:

> I think Mr. Yockey reaffirmed the fact that the Navy continued to have the [fixed-cost] requirement, and the question was, could the deficiencies be corrected so that essentially the Navy's requirement could be satisfied. Mr. Anders responded by saying we're not going to be able to address those deficiencies by 2 January. All of the deficiencies that had been pointed out cannot be corrected. Mother Nature, or

[27] Pub. L. No. 85-804 authorizes the President of the United States to grant agencies the power to provide extraordinary relief in furtherance of national defense. 50 U.S.C. § 1431; *see McDonnell Douglas*, 50 Fed. Cl. at 314 n.2.

> laws of physics or what have you, will not allow all of those to be corrected, they'll do the best they can, and the Navy was going to have to decide whether that's good enough.

Plaintiffs asked Admiral Morris about oral communications he had with the contractors' representatives prior to January 2. He testified to "three or four specific meetings or telephone discussions with both [contractors]. ... I believe they were using me as a sounding board for various ideas they had, in terms of the response to the cure notice...."

Admiral Morris encouraged plaintiffs to address the problems of cost overruns, which he said was a "real issue," though he knew the contractors were bound to a fixed-price incentive contract. He added, "[t]he contractors had clearly articulated during these meetings that they would require extraordinary relief under 85-804, or-and/or, at times, a restructure of the contract, which I believe had to take place under the authority of Public Law 85-804."

The contracting officer discussed some of the technical issues:

> [T]here was much follow-through that had to take place on the part of the contractors to address the issues that had been identified there and, of course, there were many milestones ahead, including first flight and the OPEVAL and TECHEVAL, and all of the technical reviews that would assure that the Navy was getting its desired aircraft....

Admiral Morris said the main issue with the schedule was, "when is all this going to take place? When are we going to get the aircraft that had been contracted for? ... I was encouraging that realism be addressed and that we get everything on the table so that we can proceed and go forward...." Asked about possible alternatives to 85-804 relief, Admiral Morris said this:

> It was very hard to put a boundary around each of the issues, if I may categorize them as cost, schedule and performance. I was certainly seeking an opportunity to try to address each of those issues if, in fact, they could be addressed within the contract itself, without going forward with extraordinary relief and without having to restructure that contract ... which I did not have the authority to do and which would require 85-804 relief ....[28]

The contractors met with government officials many times in late December to discuss the A-12 contract. At one such meeting, Assistant Secretary of the Navy (Research, Development, and Acquisition) Gerald Cann stated that the "Navy needs the A-12." He added, however, "[b]oth companies have failed cost, schedule and performance." He urged the contractors to respond to the cure notice because the

[28] The contractors' financial condition is a factor of importance in reviewing issues that may have contributed to justifiable default termination. *See McDonnell Douglas*, 323 F.3d at 1017. Admiral Morris testified that he was "in no position to judge the seriousness of the financial situation of either firm at that particular time...."

Navy "need[s] to get back to SECNAV by 2 Jan, show cause to SECDEF by 4 Jan." The Navy reported that it "want[s] to proceed with FSED and Lot I."

Secretary Yockey announced that the Secretary of Defense wanted a report on the program by January 4. Mr. Yockey said the Secretary was "disturbed by program problems." Mr. McDonnell stated that they "[m]ust work out of [the] problem together," but emphasized that the contractors were "not in default." He asked, "where [do] we go from here? Is there a way to go together?" Mr. Anders agreed, stating that "[b]oth contractors and Government signed [the] contract. It won't work if we don't solve [it] together."

Other important points from the minutes of this meeting relate to negotiations regarding restructure of the contract. Mr. Anders wondered why the Government could not address a general solution. "We jointly created a bad contract. [The] Government has a responsibility also to fix the contract." Mr. Anders noted that a "year ago[, the] Government estimated the contractors [were $] 1.0 billion above ceiling.... We have a mutually bad deal."

Mr. Cann informed plaintiffs that the Government's "response will depend on what contractor[s] propose." He told them to "propose what loss you will take. Government is not going to walk away from [a] valid contract. There is a way under the law to deal with it-[the] Navy has to convince OSD, who has to convince SECDEF, who has to convince the Congress."

Secretary Yockey raised the contractors' complaint that they were not receiving sufficient pro-

gress payments quickly enough, and the suggestion that conversion to a cost-type contract would reduce the problem. As transcribed from the notes, Mr. O'Donnell, General Counsel of DOD, remarked, "You estimate the EAC [Estimate at Completion] at 7.5B[illion dollars] for progress payments. [That's] a 2.5B[illion dollar] overrun!"

Mr. Anders returned to the problem that Admiral Morris referred to as "physics." Morris' notes of Anders' comments state, "Mother Nature remains a real challenge-[we are] on the edge of state-of-art. Tough to nail down future costs."[29]

Notes of a Government-only meeting following the meeting with the contractors shows that government officials disagreed about how they should proceed. Secretary Cann wanted the "contractors to tell us what they can do. I don't want to provide [the] contractors our minimum requirements.[30] I want to hear what they have to say first."

Ms. Spector thought they should provide "minimal requirements" to the contractors. "If we don't give them any indication of what could be acceptable, they may be off the mark." Secretary Yockey agreed with Mr. Cann that they should not "provide any basic requirements" as a first response. "Lets hear from

[29] This was a key problem throughout, recognized by all parties: The Government should not have attempted this project with a fixed-price contract; neither, of course, should the contractors have agreed to attempt it.

[30] The officials are discussing a possible restructure of the contract here. The reference to "minimum requirements" refers to the Government's demand for consideration from plaintiffs.

them first. Its important that they think the problem through and tell us what they can or are willing to do." Ms. Spector persisted: "We need to list five or six basic things that need to be addressed. They may only cover some of them if we don't." Mr. O'Donnell observed that PL 85-804 relief would be "distasteful," and the contractors should know it. Under Secretary Yockey agreed, adding, "[t]hat, combined with risks, indicate [the] contractors really have to make progress quickly."

The parties met again on December 21. Meeting minutes reveal that the contractors' financial situation and the state of the A-12 Program were among the Government's concerns going forward. Mr. Anders of General Dynamics understood the situation precisely, it turns out. He offered the following remarks:

> I have reflected a lot on the last meeting. Rumors abound. You can hear any you want. I hear how important the program is, how much the Navy needs it. It's reassuring if that's the position we are in, but others say we are going through a "kubuki dance"[31] preparatory to a formal termination of the program. Is it really a *fait accompli* that the program is dead? Are there really two alternatives available?

[31] The reference to "kubuki" is not explained in the record. We understand the term to be Japanese, referring to traditional Japanese theater distinguished by elaborate makeup. It seems from the context that Mr. Anders was expressing concern that the Government might have been "stringing them along."

Secretary Cann assured Mr. Anders that the Program was not "dead" if the Navy and the contractors could somehow convince the Pentagon to continue. Secretary Yockey added, "[i]t's a question of whether the program in its current state can satisfy the requirement. The question is, can you correct deficiencies to provide an aircraft that meets the requirements?"

The contractors had to demonstrate for the Government that they could perform according to A-12 contract requirements, despite setbacks that had already taken place. Mr. Anders attempted to describe the contractors' difficult task with respect to this research and development effort, urging the Government to understand that "[t]his is the state of the art. We can't guarantee in detail what the aircraft will do. We don't know the unknown unknowns." He assured the officials that nonetheless, "[h]aving been burned badly on large composites, we think we are out of the woods. All we can do is bust our tails."

The conversation turned to the contractors' financial situation. Secretary Yockey noted that the Government would not "take unlimited responsibility." He advised the contractors to "respond to the show cause [and to] articulate what you would like to do. In doing so, make sure you're taking responsibility and some continuing responsibility. If we consider it has merit, we will entertain your proposition."

Cost remained a concern, as did the fixed-price contract. Mr. McDonnell responded to criticism of the Secretary of Defense and others about plaintiffs' management issues as well. He said:

> The fixed price nature of the contract precluded good management. I did a study four years ago indicating we were heading down a slippery slope with fixed price contracts. We are not in the business of winning lawsuits. We would rather build airplanes. If we can work this out, we'll unleash everything on the Hill that we can to help.

Mr. McDonnell said the Navy should not terminate "because [it] think[s] Congress won't go along" with 85-804 relief.

Secretary Yockey reminded the contractors that the basis for the notice to cure was the contractors' not making progress. He felt the Government "ha[d] the right to terminate for default." He had a different worry about the prospect of negotiating with the contractors. That is, Mr. Yockey was concerned about whether the system would meet the Pentagon's needs in any event: "The worst problem is that if we were to propose a solution, we could end up with a product that didn't meet our requirement. I have concerns that the airplane will do all you need it to do."[32]

The Government held another closed-door meeting immediately following the briefing with the contractors. Minutes of this meeting and others showed a disconnect between the Pentagon and the Navy.

[32] This is one of the issues the contractors would have wanted to pursue, presumably, had Mr. Yockey been available to testify in court. We have not located a record of Plaintiffs' having queried Admiral Morris about this comment during trial.

For example, the Navy felt that OSD personnel were impinging upon some of the Navy's areas of responsibility.

3. OSD v. Navy

The Navy and the Office of the Secretary of Defense were at odds regarding the A-12 Program in a number of respects, including the Pentagon's handling of the termination. At a closed-door meeting, Navy official Gerald Cann said he felt the contractors "kn[ew] what kind of solution they need to provide, [but][t]hey are working serious cash flow issues. If we were to [terminate for default], we would cause major problems for them." Under Secretary Yockey's view was more practical, or perhaps pragmatic from the standpoint of OSD.

The meeting minutes describe the following exchange:

> Cann: "We need to give you a technical brief. We have gone through 1-1/2 years of critical design review[ ](CDR). The deficiencies are being addressed. We have growth areas in the plane. Trade offs will be made in terms of capabilities as long as our needs are met. This always occurs in a development program."
>
> Yockey: "I will want to get a certificate of technical adequacy from both Navy and contractors. We have to make sure the product is suitable for our needs."
>
> Cann: On [January] 3rd, I want to get my technical group over here to brief you so

> that you know where were are coming from. The technical issues have come together. There's still some risk but it's coming together.
>
> Yockey: "It bothers me that we go out with a specification that we say is our requirement [yet] we never get it complete, such as in this case the weight of the aircraft which affects other requirements." [33]
>
> Cann: "We lay out a specification that we want and think is necessary. We don't always know that it can be achieved. That's why we have development-need to make trade-offs to achieve overall requirement."
>
> Yockey: "Why did we ever go out on a fixed price contract? We should have learned long ago that you can't develop complex systems to a fixed price."

They agreed that no one wanted to suggest the Government encouraged the contractors. Mr. Cann remarked, "[e]ven though we don't know what they are going to do on [January 2], I don't want to be in a position of having encouraged them to do one thing or another. We need to hear from them." Secretary Yockey concurred: "I don't want to be in a position of

[33] The Navy was comfortable with the A-12's weight, which it accepted. The Navy waived contract specifications that required a lighter airplane. *See supra* note 26. The focus on weight was a major disconnect between OSD and the Navy, and a reason for the appearance that Pentagon officials terminated the contract without understanding facts well known to the Navy.

encouraging them to do one thing or another. We need to hear from them and then put together a strategy of what we would recommend for [the Secretary of Defense]."

Government officials discussed business issues in depth. Secretary Yockey estimated that the A-12 contract's cost to completion would be between $8 and $12 billion. They considered whether the contractors could handle loss of this magnitude.[34] Mr. Yockey understood how desperate the contractors were for cash. He believed the contractors could not continue performing with such losses; he did not want the losses to be shared equally between the contractors and the Government. He felt the Secretary of Defense "has to send strong message to industry."

4. Contractors Respond to Cure Notice

The contractors responded to the Navy's cure notice on January 2, denying they were in default of the A-12 contract. They asserted that the unilateral schedule was not enforceable and the contract speci-

[34] They could not handle such a loss. Mr. Lamers of General Dynamics made the following comments at a meeting of contractors:

> [W]hat are we going to do to resolve this impasse with the Navy? Right now, we have the two chairmen of the two companies are in continual communication with Navy acquisition executive, who is Gerry Cann, and they are working with him to come up with an acceptable package or agreement that will recognize the fact that while the contracts are behind schedule, and therefore in a dollar overrun situation, the contractor cannot absorb all those all that overrun,....

fications were not achievable. They added, "[w]hile the contractors will not meet the delivery schedule or certain specifications of the original contract, or the revised FSED delivery schedule ... for the reasons set forth below, the contractors are not in default of the A-12 contract."

> As the Program has developed, it has become clear both to the Team and to the Navy that the schedules and certain of the specification requirements, such as weight, were impossible to satisfy.
>
> ...
>
> The Contractors have been forthright with the Navy through this Program in surfacing problems as they have developed. We have worked with the Navy in good faith to overcome these problems and to deliver the best possible aircraft. The Navy cannot now ignore the fact that it has been informed of the difficulties, or that it has encouraged the Team to continue performance despite its knowledge that the delivery schedules and the literal terms of certain specification requirements were not achievable, nor can the Navy deny that the Team, in reliance on those encouragements, has diligently prosecuted the work at enormous expense to both companies.
>
> ...
>
> [T]he Team has been fully committed to the success of the Program, and has diligently

> prosecuted the work relating to fabrication of parts and all other aspects of performance in a manner that reasonably assures a satisfactory completion of the FSED and production phases of the A-12 Program.

Much of this comports with the court's understanding of the case. The contractors certainly cooperated with the Navy and they worked closely with each other to "surface[ ] problems as they developed." A review of the record shows that overall, this was more a dispute between the Navy and OSD than one of Government versus Contractors. The contractors offered the following assurances:

> First, with respect to the design and manufacturing process, the Team has made significant progress in the past several months. Nearly all structural drawings have been released to manufacturing. Since July 1990, 2,030 tools have been completed. Manufacturing processes and yields are dramatically improved.
>
> ...
>
> Second, the Team has made major advances in the A-12 Test Program. Wind Tunnel tests are 92% complete, well ahead of need as measured against current schedules.... Survivability and vulnerability testing, not even required for first flight, is 77% complete, and all tests will be complete prior to first flight.

Third, ... substantially all of the approximately 20,000 procured line items will be available to meet manufacturing need dates, and, as of November 30, 1990, 95% of Aircraft 1 procured requirements have already been purchased and delivered.

...

The [cure] notice ... states that the Team's alleged "failure to meet specification requirements, such as aircraft weight, jeopardizes the carrier suitability of your design." The team's design for the A-12 was found to be technically sound during the exhaustive Critical Design Review. While there is a shortfall against some parameters of the original technical specification, we believe that the current design meets the operational objectives.

...

[D]espite the exceptionally difficult technical challenge presented by this revolutionary design, during the Design Review Board (DRB) process that was completed in October 1990, the Team convincingly demonstrated that the A-12 design is technically satisfactory. Over 400 significant technical issues were addressed and resolved during this DRB process.

...

> [C]ontractor development and manufacturing activities have been substantially and excusably delayed and impacted by acts and omissions of the government. Very important information vital to the performance of the contract, available to the Government, was not provided.... For those same and other reasons, the schedule unilaterally imposed by the Navy is also not valid; and, furthermore, it is unreasonable inasmuch as it purports to schedule FSED aircraft deliveries after delivery of Lot I aircraft.

The contractors concluded:

> We provide this response to demonstrate our commitment to the Program, and specifically to address the concerns you have raised. Our greater objective is to conclude successfully an equitable restructure of the contract and clear the way for the design and delivery to the Navy of superior new attack aircraft....

The contractors' response accompanied a separate "Proposal for Equitable Restructure of the A-12 Contract." They asked that the contract be converted to cost-reimbursement and agreed to absorb a $1.5 billion loss on the contract in return. They would waive all claims for equitable adjustments of approximately $1.6 billion. Cash flow to the contractors would be made on the basis of flexible progress payments, and the parties would restructure the contract so that

procurements subsequent to Lot I would be subject to separate, future stand alone contracts.[35]

5. The Weekend

The Chief Engineer for the Navy reported at a meeting with Admiral Morris on Friday, January 4, that technical challenges on the A-12 were typical for this type of development contract, and that the contractors could resolve the remaining technical challenges. The Navy and the Joint Requirements Oversight Council had revalidated the operational requirements.[36] Despite this optimistic assessment of progress in resolving technical problems, OSD seemed determined to close down the Program.

The Secretary of Defense met with Navy Secretary Garrett, Under Secretary Yockey, and the Chairman of the Joint Chiefs of Staff on Saturday, January 5 and decided not to grant 85-804 relief.

[35] Secretary Yockey had no concern that the contractors were incompetent or otherwise unable to handle the A-12 contract; he was worried about the appearance of a "bailout" if he allowed plaintiffs to continue. He would have been willing to go forward if the contractors could have accepted a $2 billion loss and made other concessions. *See McDonnell Douglas,* 50 Fed. Cl. at 314 n.3 (concluding that Mr. Yockey, the major decision-maker on the scene at the time, was merely "haggling over price.").

[36] This optimistic assessment was the contracting officer's last official report on the status of the A-12 Program before Monday, January 7, when he terminated the contract for default. The Joint Requirement Oversight Council, or JROC, consisted of members from the Joint Chiefs of Staff. JROC conducted its own review of the A-12 requirements and concluded that the aircraft "satisfies all mission requirements." *McDonnell Douglas,* 35 Fed. Cl. at 363.

Secretary Cheney knew the A-12 Program would be cancelled as a result, but he testified that the Navy would decide whether to terminate the A-12 contract.[37]

Admiral Morris was not invited to the Defense Secretary's meetings with top military personnel on Friday and Saturday, and he did not know of the meetings' outcome. He was called in to meet with Secretary Yockey and other Department of Defense officials on Sunday, January 6. Secretary Yockey told Admiral Morris that Secretary Cheney would not provide 85-804 relief.[38] Yockey told Admiral Morris that he, "as the milestone decision authority, can no longer support the program because of cost, schedule, [and] performance problems, and I will not authorize the obligation of any additional funds for the program." [39]

[37] This distinction resolved an apparent dilemma among counsel for defendant and for OSD regarding the role that the OSD was to have played; i.e., whether the Secretary was to have been removed from decision making regarding termination, or involved, and to what extent.

[38] This is another circumstance about which plaintiffs surely would have wanted to question Mr. Yockey. We inferred that Admiral Morris received his instructions regarding default termination at this meeting.

[39] Secretary Yockey, the person who carried the termination message to Admiral Morris, who played a major role in causing the contracting officer to terminate the contract he wanted to continue, and whose name appears on many pages of this Opinion, did not testify in any court proceedings. We found after the Count XVII trial that Mr. Yockey "recommended against both 85-804 relief and the continuation of the program because the contractors were not willing to accept a sufficient loss on the

That Sunday afternoon, Admiral Morris contacted NAVAIR's Navy's legal counsel, Margaret Olsen, to tell her he was prepared to terminate the A-12 contract. He terminated the contract for default the next day.[40] The contractors were due an installment of $553 million the same day, January 7, 1991.

The contracting officer's termination letter to the contractors stated:

> General Dynamics Corporation and McDonnell Douglas Corporation (hereafter Team) are in default of [the] Contract.... The Government, therefore, is terminating [the Contract] in accordance with FAR

contract .... [and] that 85-804 would look like a bailout of the contractors." *McDonnell Douglas*, 35 Fed. Cl. at 365. The only route Yockey thought appropriate was termination. He wanted to terminate for default immediately, before more funds were obligated. *Id.*

[40] Following his meeting with Secretary Yockey, Admiral Morris contacted his supervisor, Admiral Gentz, and told him that the Defense Department would not authorize Public Law 85-804 relief, and that Secretary Yockey had withdrawn his support for the Program. This was Admiral Morris' last-ditch effort to save the Program. He hoped Admiral Gentz would encourage the "big guns" in the Fleet to try one last time to save the A-12. Despite this lack of high-level support, Admiral Morris wanted an opportunity to continue development. He laid out reasons for continuation without extraordinary relief. He did not think additional funding was the only way to sustain the Program, and he wanted to work with the contractors. On the day before termination for default, despite being denied "extraordinary relief," the contracting officer wanted to continue the contract. The same afternoon, however, he called a NAVAIR attorney to alert her concerning the likelihood of termination. The next day, he terminated plaintiffs for default.

> clause 52.249-8, "Default (Fixed-Price Supply and Service)" and 52.249-9, "Default (Fixed Price Research and Development)." ...
>
> This action is based on the Team's inability to complete the design, development, fabrication, assembly and test of the A-12 aircraft within the contract schedule and the Team's inability to deliver an aircraft that meets contract requirements.

Neither Admiral Morris nor his counsel had the time to put together a termination letter for the contractors and a termination memorandum to justify the Government's action for the file. Some of the reasons for termination used in the memorandum resulted from directions of OSD's legal department. As a result, both documents cited reasons for default that previously the Navy had not considered reasonable bases for such action. The Navy had worked side-by-side with the contractors for many months preceding termination to resolve technical difficulties inherent in designing a plane that would be stealthy, yet land on an aircraft carrier and meet other needs of the Navy.

Ms. Olsen prepared a termination memorandum in the early morning hours on the day of termination. She did not have much information about the A-12 contract at her disposal, so she used a termination letter from a previous Navy program as a template. She had not anticipated terminating the A-12 for default. Ms. Olsen used the P-7 for more than a baseline, however. She looked to language from the P-7

for substantive reasons for terminating the A-12, a major research and development procurement, for default. Thus, the contracting officer's termination memorandum for the A-12 reflects an analysis conducted for the P-7 program, not the merits plaintiffs' performance on the A-12. Language in the P-7 memorandum is identical to language of the A-12 document.[41] Ms. Olsen was questioned about the similarities when she testified:

> Q: Now, let's look at the further statement for "two or more years' delay in the completion of development," do you see that phrase?
>
> A: Yes.
>
> Q: Do you know where you got that?
>
> A: No, I don't recall.
>
> Q: Now, Ms. Olsen, that's exactly the language that you put in the Lockheed [P-7] memorandum, isn't that right?
>
> A: Yes.
>
> Q: Is it also possible that you had not verified that two or more years was appropriate to the A-12?

[41] The P-7 memorandum stated, "Lockheed has made no case that two or more years' delay in the completion of development is other than Lockheed's fault...." The A-12 Memorandum included the following: "[t]he Team has made no case that ... two or more years' delay in the completion of development is other than the Team's fault."

> A: And it's also possible that two or more years was the amount of delay projected in both programs.
>
> Ms. Olsen had no idea what the basic issues involving the A-12 were, and did not have time to find out. Whether the contractors were two or more years behind is an important aspect of the case before us now.
>
> Ms. Olsen was aware of correspondence between the contractors and the Navy, but had not seen the contractors' claims or their response to the cure notice. Her staff gathered information on the A-12 Program. She did not discuss the basis for termination with Admiral Morris. She did not seek information from the chief engineer, the program manager, or any technical personnel. She did not discuss the termination letter with Admiral Morris, though he issued it to the contractors later that day.[42]

Admiral Morris' January 7 termination memorandum for the file was an in-house document that explained the rationale for termination:

[42] "Morris approved the termination memorandum at midday after less than an hour of review." *McDonnell Douglas*, 35 Fed. Cl. at 368. The A-12 termination memorandum did not reflect any contracting officer analysis of the time when the A-12 contractors were likely to complete the remaining contract effort. *See Id.* ("[Admiral Morris] did not review documents related to schedule or specifications.").

After considering the factors set forth in Federal Acquisition Regulation 49.402-3(f), I have determined to terminate this contract for the default of the Contractor.

...

The contract includes the [default] clause ..., which can be found at FAR 52.249-9; and this clause, at paragraph (a)(1)(iii), provides that the contract may be terminated for default if the contract so fails to make progress as to endanger performance of the contract. As outlined below, the Contractor's performance evidences an inability or unwillingness [43]of this contractor to meet the requirements of the contract. The team has made no case that three to nine months further delay in the delivery of the first aircraft or two or more years' delay in the completion of development is other than the team's fault, or that it is entitled to be relieved of the performance requirements of its contract.

Specifically, the team cannot deliver the first prototype aircraft required ... in December 1991. Since June 1990, the team has consistently reported its delays; and the Navy's independent review confirmed that, given the state of the team's

[43] No one else has suggested that the contractors were "unwilling" to build this aircraft. Admiral Morris certainly knew better. Presumably, Ms. Olsen copied that clause from the P-7 template.

development efforts, delivery of aircraft and completion of related contract requirements could occur no sooner than .[sic].[44]

The importance of this delay cannot be overstated. The production options must be exercised by dates certain to be enforceable. As a consequence of the team's delay, the Navy would be required to purchase production aircraft before verifying that the aircraft are operationally suitable and effective[45].... Moreover, the delay so increases the cost to the team of completing the contract that it casts doubt on their willingness to perform.

Specifically, the team cannot meet the performance requirements of the contract. The team is currently designing the aircraft to have a weight empty 7930

[44] Despite his assertion that "[t]he importance of this delay cannot be overstated," the contracting officer did not know what the delay was. Yet the contractors and the Navy had discussed estimates for first flight. The Navy had told Secretary Cheney that the first flight date was expected in September 1992. Navy witnesses agreed that the September 1992 date was realistic and acceptable.

[45] The A-12 contract required that the Navy exercise all options to purchase production lots "before verifying that the aircraft are operationally suitable and effective." This justification therefore either was taken from the P-7 or invented by someone. A witness for the Government, Eleanor Spector, testified that this element of the contract schedule was a "risk" known before the contract award, and not "a consequence of the team's delay."

pounds in excess of the guaranteed contract weight empty. This additional weight precludes the team from meeting contract requirements for takeoff distance, cruise specific range, maximum airspeed, and fuel flow, all of which directly affect mission capability.[46]

Excuses offered by the team are as follows. First, the team contends that its development and manufacturing activities have been substantially affected by acts and omissions of the Government. Specifically, the team alleges that the Government failed to provide "very important information vital to the performance of the contract" that was available to the Government. Second, the team alleges that necessary risk reduction prior to the award of a fixed price development contract was not present in this effort. Intertwined is the argument that meeting the required weight called for by the specification is impossible.

Third, the team argues that its obligation to perform is limited to amount of funds available, provided through incremental

[46] Weight was not a problem for the Navy at termination. The design review process described earlier insured that the plane could take off and land on a carrier and otherwise would meet the Navy's stringent requirements for such a system. Using weight as a reason for termination was not Admiral Morris' idea, nor Ms. Olsen's, but that of the Office of Secretary of Defense.

> Government funding. Finally the team argues that the schedule is not valid and is unreasonable because it purports to Schedule FSED aircraft deliveries after delivery of Lot I aircraft.

The termination memorandum continued by addressing the contractors' assertions in response to the cure notice.

> The Government has provided the team all information relevant to the performance of this contract that the Government was required contractually to provide....
>
> The weight guaranty in the contract specification was provided by the team. The team is currently projecting weight at 7930 pounds over the required weight which critically calls into question the aircraft's suitability for carrier operations. The added weight impairs the Aircraft's single engine rate of climb and increases substantially wind over deck requirements; both serious considerations for carrier operations. The team has provided no valid excuse for not meeting the contract weight that it submitted and agreed to meet.
>
> This contract is a fixed price contract that requires delivery of conforming goods by a date certain conditioned on the Government allotting funds in the amounts and at the times stated. It is not a cost type of contract where the contract is only

> required to work to the limit of available funds.
>
> Finally, the overlapping schedule of FSD and Lot I deliveries does not relieve the team of the requirement to meet either Schedule. The FSD schedule was extended after the team failed to meet the original Schedule in the contract. The Lot I schedule could not be extended at the same time because too much uncertainty surrounded the team's ability or willingness to perform to any Schedule.
>
> In summary, the team's failure to make progress and to deliver an aircraft meeting required weight has placed the entire program in jeopardy; and the contractors have offered no adequate excuse for these failures.

Mr. Cann's January 8, 1991 handwritten notes include this retrospective judgement: "Uncertainty was what did it in...." Perhaps, but the decision to terminate the A-12 contract was driven by the $553 million progress payment that the Navy was to obligate on the same day. The Government's largest procurement ended in a weekend effort by Department of Defense officials to avoid the Government's own default by failing to release half-billion dollars to plaintiffs on Monday, January 7, 1991.

E. LITIGATION HISTORY

The United States terminated its contract with McDonnell Douglas and General Dynamics, citing the contractors' inability to meet contract require-

ments and failure to make progress.[47] Plaintiffs sued to convert the termination for default to termination for convenience of the Government. Following trial, we ruled that the Navy's termination process was not a reasoned one and that the contracting officer had not been permitted to exercise the independence required of him by Federal Acquisition Regulations.[48] *McDonnell Douglas,* 35 Fed. Cl. at 368-73. Testimony and other evidence at the first trial showed that Ad-

[47] The contracting officer issued a final decision pursuant to the Contract Disputes Act, stating as follows:

> On 17 December 1990, the Navy informed the Team that it considered conditions under the contract to endanger performance and asked the Team to cure those conditions. Having carefully considered the Team's 2 January 1991 response, I conclude that the Team has failed to explain or cure those conditions, and that the Team is in default of the contract for having failed to make progress and not meeting contract requirements. The A-12 aircraft will not be delivered within the contract schedule nor will it meet the weight guaranty contained within the contract specification.
>
> ...

This is the final decision of the Contracting Officer....

[48] The contracting officer is a government employee with the responsibility of administering a contract for the contracting agency. Federal regulations require that he or she act as an independent arbiter to resolve disputes that arise with the contractor by "safeguarding the interests of the United States in its contractual relationships .... [while] ... [e]nsur[ing] that contractors receive impartial, fair, and equitable treatment." FAR 1.602-2. We were impressed with the contracting officer in this case, a well-regarded, high-ranking naval officer who nevertheless was unable to administer the contract according to his best judgment.

miral Morris terminated the contract mostly for reasons we thought unrelated to performance.

Defendant argued initially that government officials could have terminated the contract in Admiral Morris' stead, and had the authority to act on the contracting officer's behalf in any event. We stated, "[p]erhaps [other government officials] could have terminated the contract-we had no reason to address this issue.... [T]he Government offered no individual or entity other than the contracting officer as the decision-maker. In fact, defendant's witnesses disclaimed such a function during trial." *Id.* at 372. Defendant apparently abandoned that legal position later, and took pains to disclaim such activity by other government officials.[49]

The first opinion on this issue described the process leading up to termination in some detail to explain why it appeared that Admiral Morris did not make an independent decision to terminate the Program for default on the same day that he had been

[49] Defendant argued that the role OSD did play in the termination did not nullify the default termination, however. According to defendant, the termination for default was the " 'direct consequence of a legitimate exercise of OSD's statutory and regulatory oversight authority; [t]hat the discretion of the contracting officer regarding contract continuation may have been obviated by OSD's actions is of no consequence.' " *McDonnell Douglas,* 35 Fed. Cl. at 372. We had misgivings about that argument at the time, but rulings since then may have vindicated the Government's position. The matter did not arise again, however, because later the Government denied any influence or other actions on the Secretary's part.

lobbying the Fleet for support to keep it going. [50]The ruling of the Court of Appeals for the Federal Circuit that Admiral Morris terminated the contract for performance-related reasons and exercised independent judgment apparently derived from Admiral Morris' testimony at trial. *McDonnell Douglas Corp. v. United States,* 182 F.3d 1319, 1327-28 (Fed. Cir. 1999).[51] The court found that it could be guided by Admiral Morris' testimony, stating:

> [The contractors] were in default because they acknowledged they would not be able to achieve the contract specifications and

[50] Admiral Morris was impressive as a conscientious witness and a flag officer of the United States Navy. Given the Federal Circuit's conclusions on remand, we must assume that once Admiral Morris understood the importance of the Government's right to terminate in the circumstances presented to him, he then conducted the necessary reviews and made a reasoned decision to terminate for default.

[51] The Navy and the Secretary of Defense disagreed in their assessments of the A-12 Program and their willingness to tolerate delay. The Navy wanted the A-12 for its Fleet and was prepared for compromise. The Secretary had other concerns and was more critical of the Program. According to the Circuit:

> The trial court's factual findings do in fact establish that the Navy did not want to terminate the A-12 Program. Instead, at all times up until the very end, the Navy hoped to preserve the Program and its A-12 aircraft. That is not to say, however, that Contractors were not in default under the contract, or that the Government did not have the right to terminate for default.
>
> *McDonnell Douglas,* 182 F.3d at 1327. The appeals court concluded that the Navy's reluctance to terminate the contract was indicative of the serious nature of the contractors' default. *Id.*

> the contract requirements, ... the[y] would not be able to meet the delivery schedule that was currently in the contract, [a]nd ... they would not be able to perform the contract without extraordinary relief or additional funding for the contract. So they basically said they can't perform under the contract and they were in default of it.

Id. at 1327. He said he believed the contractors could not complete the project within the time allowed for performance. The Circuit noted Admiral Morris' testimony with approval:

> [A]s a result of the contractors' default, it would be nothing short of unconscionable for me to put the burden of the contractors' failure to make progress and the contractors' failure to fabricate parts, so as to endanger performance of the contract, put that burden on the Government and the taxpayer to reimburse all costs and to pay the contractors a profit for their failures.

Id. at 1328. The appeals court made the following conclusion from Admiral Morris' testimony:

> [Admiral Morris] thought that he had three choices: to terminate for convenience, to terminate for default, or to do nothing. He rejected the latter as 'irresponsible,' thus focusing his attention on the other two choices. He eliminated the termination for convenience first, because he believed

Contractors to be in material breach of the contract.

Id. at 1327. Thus, Admiral Morris terminated the contractors because he believed that they were in default of the A-12 contract, and it would have been unconscionable and irresponsible for him to terminate for convenience or do nothing.

The Circuit's remand order stated that the court so far had addressed only procedural matters and directed trial on whether the contractors were actually in default at termination. The burden of proving plaintiffs were in default was on the Government, which offered justifications for its termination of the A-12 contract during the six week default trial that ensued. The parties did not try this case on the *Lisbon* test, but on the contractors' failure to meet the contract schedule. We had ruled earlier on the Government's other reasons for terminating plaintiffs for default: weight of the aircraft, plaintiffs' financial status, and repudiation or abandonment. It appeared then that schedule was the only issue remaining.

The modified schedule called for first flight nearly a year after the Government terminated plaintiffs for default, but first flight was only an "interim deadline."[52] The contractors and the Navy had known

[52] First flight was important and significant to those close to the A-12 contract. The significance arose from the parties' negotiations in the months leading to termination. The contractors' ability to conform to the first flight schedule had been a bellwether of sorts, and a concern of government officials. First flight was the first test. Missed milestones may be considered in

that plaintiffs would not make first flight, so the issue for trial was whether the unilateral schedule known as P00046 was reasonable and enforceable. A unilateral schedule must be reasonable to be enforceable, so testimony centered on whether the Navy was reasonable in imposing a December 1991 first flight deadline.

Testimony showed that the schedule was reasonable, and we entered judgment for the Government. The Federal Circuit ruled on appeal, "finding that the unmet first flight date in December 1991 was reasonable is insufficient to sustain a default termination in this case." *McDonnell Douglas,* 323 F.3d at 1014.[53] The Circuit explained, "[i]n determining whether a default termination was justified, [trial] court[s] must review the evidence and circumstances surrounding the termination, and that assessment involves a consideration of factual and evidentiary issues." *Id.* The appeals court vacated the judgment and remanded for review of whether the default ter-

conjunction with other factors in weighing the contracting officer's decision to terminate for failure to make progress.

[53] We did not find that the due date for first flight was "unmet." If it had been, perhaps the issue would have been analyzed differently. This is important because the Government terminated plaintiffs almost a year prior to first flight. At termination, January 7, 1991, the parties understood that McDonnell Douglas and General Dynamics would not deliver first flight a year later, in December 1991. This is the reason the second trial focused on enforceability of the unilateral schedule. If the unilateral schedule had not been found reasonable, it would not have been enforceable.

mination was justified according to the *Lisbon* standard. *Id.* at 1015.[54]

This brief summary of developments in this case is limited to matters directly antecedent to this issues presented. These are the nature of the contract; the contractors' performance before termination, in-

[54] The Circuit did not express an opinion on whether we should reopen the record; the matter would be left to the sound discretion of the trial court. For that reason, we asked the parties repeatedly whether they recommended additional trial. Plaintiffs and defendant opposed reopening the record or taking additional testimony for any purpose. The parties agreed that the court has sufficient information in the trial record to rule on remand. Though the Federal Circuit expressed its inability to rule on "an incomplete record," the court was referring to the appellate record, according to defendant. Government counsel explained during a hearing last year:

> [T]he Federal Circuit told us that the appellate record before it on the last appeal was inadequate to answer [the question of whether the Government justifiably default terminated the contractors for failure to make progress], so it had no choice but to remand the case back to this Court....
>
> All of the answers to those questions were in this trial court record.
>
> Unfortunately, because of the way the arguments got briefed and the appendix assembled for the Court of Appeals, the answers to those questions and the necessary documents from this trial court's record were not included in the appellate record, so the Court remanded it.
>
> Government counsel also expressed concern during a hearing last year that additional trial may be needed to address defendant's claim for a loss adjustment. That issue is moot now, given the judgment we enter today.

cluding the contract schedule; events leading to termination, including a number of earlier factual findings that are relevant to contracting officer's testimony and contemporary evidence; and the litigation that resulted from the Government's termination of plaintiffs for default. It does not address separate trials concerning matters raised by plaintiffs' complaint, or dispositive orders and other rulings on coordinate issues. The issue remaining is whether default termination was justified according to the *Lisbon* standard.

II. DISCUSSION

Default termination is a "drastic sanction ... which should be imposed (or sustained) only for good grounds and on solid evidence." *J.D. Hedin Constr. Co. v. United States,* 187 Ct. Cl. 45, 408 F.2d 424, 431 (1969) (internal citation omitted). Termination is a forfeiture that is disfavored in the law and to be construed narrowly by the courts. *DeVito,* 413 F.2d at 1153. The Government must prove default: "If the [G]overnment can establish that [the] Contractors were in default, then the termination for default would be valid." *McDonnell Douglas,* 182 F.3d at 1329 (citing *Lisbon,* 828 F.2d at 765). This court reviews a contracting officer's decision to terminate for default *de novo.*41 U.S.C. § 609(a)(3); *see also McDonnell Douglas,* 323 F.3d at 1018 n. 3 (citing *Wilner v. United States,* 24 F.3d 1397, 1401 (Fed. Cir. 1994) (*en banc*)).

The Government's authority to terminate the A-12 contract for default derives from FAR 52.249-9, which the contract incorporated by reference. The

default section for fixed-price research and development contracts states, "[t]he Government may, ... by written Notice of Default to the Contractor, terminate this contract in whole or in part if the Contractor fails to-... [p]rosecute the work so as to endanger performance of this contract...." 48 C.F.R. § 52.249-9.

Early cases ruled that timely completion must be impossible before the agency may terminate a contract for failure to make progress. *See* John Cibinic, Jr. & Ralph C. Nash, Jr., *Administration of Government Contracts* 930 (3d ed. 1994) (noting that while the default clause uses the phrase "endanger performance," the Government was required to show that "it was impossible for the contractor to complete by the due date"). Current law does not require impossibility, or repudiation or abandonment by the contractors, but a showing by the Government of a demonstrated lack of diligence. *McDonnell Douglas,* 323 F.3d at 1015 ("[T]he default clause in this contract did not require a finding that completion within the contract's time limitations was impossible.") (citing *Discount Co. v. United States,* 213 Ct. Cl. 567, 554 F.2d 435, 441 (1977); *Universal Fiberglass Corp. v. United States,* 210 Ct. Cl. 206, 537 F.2d 393, 398 (1976)). Termination for default for failure to make progress usually occurs where the Government believes a contractor is so far behind schedule that completion of the job within the time remaining for performance is unlikely. *See Hannon Elec. Co. v. United States,* 31 Fed. Cl. 135, 143 (1994).

The Federal Circuit apparently found little agreement between plaintiffs and defendant on the standards this court should apply to a review of the

contracting officer's decision to terminate. *See McDonnell Douglas,* 323 F.3d at 1014 (noting the parties "advance[d] drastically opposite interpretations" of the FAR default provision). The contractors argued the "absolute impossibility of performance" requirement of earlier cases, but the Circuit ruled "complete repudiation or abandonment" was no longer necessary. Defendant asserted on appeal that this case presents issues of first impression: "[T]he circumstances of this case are so different that [the Court of Appeals for the Federal Circuit] should not seek guidance from precedent." *Id.* at 1015. The Government reasoned that "default termination was appropriate here given the Contractors' admitted inability to meet an interim contract milestone, the alleged impossibility for the aircraft design to meet contract specifications, and the Contractors' request for a restructuring of the agreement." *Id.*

The Federal Circuit resolved the matter with a "pragmatic approach" taken from the ruling in *Lisbon. Id.* According to the Circuit, *Lisbon* provides "the proper interpretation of the default provision [that] lies somewhere between the parties' extreme positions...." *Id.* Its pragmatic approach also achieves a desired "balance between judicial aversion to default terminations .... and the fact that the Government, just as any other party, is entitled to receive that for which it contracted...." *Id.* (internal citations and quotation marks omitted).

The Navy's default termination was justified if plaintiffs were in default of the A-12 contract on January 7, 1991. *See McDonnell Douglas,* 182 F.3d at 1329. According to *Lisbon,* plaintiffs were in de-

fault for failing to make progress on the A-12 contract at termination if the Government proves that at termination the contracting officer had a reasonable belief "that there was no reasonable likelihood that the contractor[s] could perform the entire contract effort within the time remaining for contract performance." *McDonnell Douglas,* 323 F.3d at 1016 (quoting *Lisbon,* 828 F.2d at 765). The Federal Circuit discussed the importance of "decid[ing] the actual performance that the contract requires and the amount of time remaining for performance" before deciding whether there was no reasonable likelihood "the contractor[s] could perform the entire contract effort within the time remaining for contract performance." *McDonnell Douglas,* 323 F.3d at 1017.

The remand order describes three important tasks:

> (1) finding the "entire contract effort";
>
> (2) finding the "time remaining for contract performance" at termination; [55]and
>
> (3) deciding whether the contracting officer reasonably determined that the contractors could not be expected to perform the entire contract effort within the time remaining for performance.[56]

[55] The "time remaining for contract performance" calls for a "contract completion date." This phrase in particular creates much of the disagreement between plaintiffs and defendant.

[56] Answers to the first two questions are necessary predicates to the third; that is, whether the contracting officer acted reasonably in making his default decision. Nature of the contract

A. THE PARTIES' ARGUMENTS

The contractors urge a broad interpretation of the Circuit's ruling in *Lisbon*. The appeals court used the term "entire contract effort" repeatedly and with emphasis. This must mean the court is to include eight FSED aircraft and six Lot I production aircraft in the fraction showing amount of work completed, plaintiffs contend. Their interest is in stretching the contract term out so they could clearly have met the timing requirements eventually. The longer their time remaining to complete the work, the more difficult it would be for the Government to prove contract performance was endangered.

Plaintiffs make their "entire contract" argument convincingly because the contract's "time remaining for performance" is unknown; the contractors say it is nonexistent. This is due to the nature of the A-12 contract-even beyond delivery of the Lot I production aircraft, the contract called for years of follow-on testing, aircraft maintenance, and contractor support on this major research and development effort. Plaintiffs' position is sensible. Research and development contracts typically lack clear indicia of contract completion. Their schedule guidelines are flexible, as befits the open-ended projects normally controlled by research and development contracts; often no end date applies. A witness for the Government testified, "[u]ntil you get to the end [of the contract], you don't know what the last step is."

and length remaining for performance are needed to conduct a *Lisbon* test.

Plaintiffs' other argument is that the contract completion date was waived-or disestablished-when the Government let original first flight pass in June 1990 and reset only part of the delivery schedule through the P00046 modification. P00046 included only revised delivery dates for the first eight aircraft and not the remaining contract milestones. In other words, plaintiffs maintain the Navy lost its right to terminate them for default for failure to make progress because it waived the schedule to contract completion.

The Government offers a flexible approach to review of the contracting officer's decision. Defendant contends that this court need decide only whether the weight of the evidence shows the contracting officer reasonably felt insecure about the contract's timely completion.[57] The contract contained a series of enforceable delivery dates, defendant points out; time was of the essence. The Government could terminate plaintiffs for default if the contracting officer

[57] We infer from defendant's various offerings during oral arguments and in briefs that the Government realizes that a date for contract completion was not spelled out in the A-12 contract. Dates of timely completion defendant has suggested range from first flight in December 1991, to TECHEVAL in April 1993, to CLIN 0058 in June 1996. CLIN 0058 was the final line item chronologically. Such suggestions are unconvincing for their shotgun effect, but defendant raised a plausible contention: Whether we use TECHEVAL as a mark of "essential completion," or the close of CLIN 58 as the final completion date, "performance remaining under the contract" can be tied to a particular CLIN or a specific date among the CLINs. This ruling is based on a series of dates that are tied to a particular CLIN, P00046.

reasonably believed timely completion was uncertain. Defendant argues that "entire contract effort" as used by the Circuit represents any convenient measure of the delivery dates. This measure may be used to evaluate the contractors' progress at termination.

Defendant's argument assumes an important fact: the yardstick we use to measure plaintiffs' progress is not so important as having one. That is, the "entire contract effort" need not include every segment of work contemplated by the contract, but may be any objective measure of the contractors' progress at termination.[58] Defendant's reluctance to point to a completion date was apparent during post-remand proceedings.

B. APPLYING *LISBON*

The A-12 contract contemplated a sophisticated research and development project designed to employ the United States' most sensitive technology. Such a contract does not subject itself easily to existing case

[58] This analysis is similar to the approach we took in the last opinion, however. A critical delivery date such as first flight might be considered a convenient yardstick against which to measure progress, as this was a key goal of all parties during early performance of the contract. Nevertheless, the Federal Circuit made clear that "'the Government did not, as it urges, satisfy its burden by merely showing that the contractor[s] w[ere] behind schedule.'" *McDonnell Douglas,* 323 F.3d at 1014 (quoting *Lisbon,* 828 F.2d at 765). Defendant's suggestion that we use a reasonable yardstick is attractive for its flexibility, but rulings of the Federal Circuit may call such a shortcut into question.

law from the contract boards.[59] *Lisbon* was a construction case with an identifiable contract closing date. *See* 828 F.2d at 761. Assessing the contractor's progress at termination in *Lisbon* was a straightforward calculation using work accomplished, the work left to be done, and the time left to complete it.

The central issues important to an application of the *Lisbon* standard are work left to be completed and time remaining to complete it. The parties do not agree on the meaning or significance of these potentially dispositive issues. The Circuit did not suggest an appropriate legal standard to apply, or provide a legal basis for choosing among the competing arguments. The court of appeals "le[ft] it to the trial court to determine on first instance the actual performance required by the contract and the amount of time remaining for that performance." *McDonnell Douglas,* 323 F.3d at 1018.

An alternate means of resolving this case would be to choose a closing date offered by the Government. Such dates could be CLIN 58, the latest of the suggested dates, or TECHEVAL, in April 1993. The contractors make persuasive arguments that neither alternative date would be "final." They would not

[59] The Circuit highlighted a board case in which a fraction was used to show the extent of a contractor's job performance. *See McDonnell Douglas,* 323 F.3d at 1016 (reviewing courts may "compar[e] ... the percentage of work completed and the amount of time remaining under the contract") (citing *Thomas & Sons, Inc.,* ASBCA No. 51874, 01-1 BCA ¶ 31,166, 2000 WL 1721787 (Nov. 13, 2000)). The nature of this research and development contract is such that objective evidentiary helps like a percentage of completion are not available.

cover the time needed and permitted by contract for plaintiffs to complete performance.[60]

Using CLIN 58 or TECHEVAL is artificial and arbitrary considering the failure to make progress clause. The presumptive purpose of clauses allowing the Government to terminate a contract for failure to make progress is to enable an agency to end a project before the contractors miss a delivery or fail to complete a building on time. The end date may be well before the contract's provision for delivery or completion.[61]

The Circuit commented that boards have applied the *Lisbon* test in default terminations for failure to make progress. *See Id.* at 1016 n.2. These cases apply only by analogy because they are not failure to make progress cases involving research and development efforts. The reason for this may be that the

[60] One peculiarity of this alternative is plaintiffs' need to obtain the latest date for measuring performance possible, to give them more time in theory to build the A-12. The latest date possible calls for plaintiffs to show maximum inefficiency in construction. The contractors improve their legal position by contending that the Navy would have had the right, and presumably would have needed to, seek retesting and reconfiguration to achieve the plane it wanted.

[61] Early case law calling for a showing of impossibility or near-impossibility of performance, or abandonment, before allowing default for failure to make progress becomes more understandable in this light. Terminating a contractor months before the delivery date is appropriate if the contractor has abandoned the project or repudiated the contract; otherwise, termination can be harsh, inappropriate, and unexpected. *See, e.g., Universal Fiberglass,* 537 F.2d at 398.

Government rarely terminates fixed-price research and development contracts for default.[62]

The differences between the facts of *Lisbon* and of this case highlight the difficulties of interpretation. The *Lisbon* test creates problems of application when reviewing default terminations of contracts without completion dates. A case that redefined the required showing in default terminations for failure to make progress is *Universal Fiberglass,* 537 F.2d at 397. Though itself not a research and development case, *Universal Fiberglass* provides useful principles to guide the Federal Circuit's directions.

C. UNIVERSAL FIBERGLASS

Universal Fiberglass considered a supply and service contract for more than 12,000 mail delivery trucks after government approval of a pilot model. *Id.* at 394. The Government warned the contractor repeatedly that failure to meet the delivery schedule would be grounds for termination of the contract. *Id.* The Government accepted Universal's model, but the contractor was unable to meet the first "benchmark" or milestone for delivery of production items. *Id.* The parties agreed to a ninety-day extension. *Id.* Follow-

[62] Research has uncovered only two. *See Appeals of Flight Refueling, Inc.,* ASBCA Nos. 48503, 46846, 97-2 BCA ¶ 29,000, 1997 WL 285073 (May 22, 1997) (board found a valid default termination for failure to deliver two prototypes called for as end items on a development contract); *Appeals of ISC/Phonplex Corp. Instrument Sys. Corp.,* ASBCA Nos. 16668, 16772, 73-2 BCA ¶ 10,361, 1973 WL 1903 (Oct. 31, 1973) (board held a default termination invalid because the contracting officer had waived the delivery schedule). Neither is similar to this case factually.

ing several additional extensions of time, none of which Universal met, the Government requested that the contractor submit a revised delivery schedule. The GSA Board made two rulings. First, it found that the government's request "impliedly waived plaintiff's failure to progress (so) as to endanger performance of the contract" by asking for the new delivery schedule *Id.* at 397. The Board stated also that Universal's progress failures could not include those actions prior to the Government's request for the revised schedule. *Id.*

On appeal, the United States Court of Claims reversed the board's conclusion with respect to the "failure to make progress implied waiver," stating, "[f]ailure to make progress is obviously something different from failure to deliver, or else the default clause would not provide separately for both." *Id.* at 398. The court found that the concept of waiver was inapplicable in failure to make progress cases:

> [T]he "cure notice" provision for "failure to make progress" terminations is obviously intended to supply the absence of a specific time marker to advise when the minute for default has been reached, such as exists when a contract delivery date has passed without delivery. Thus to have prescribed a new delivery schedule also would have been supererogatory. The "cure notice" served its purpose ... the contracting officer [had not] learned, from the contractor or any other source, any information to lead him to believe that deliveries would or could ever be resumed. In such

> circumstances, a unilateral delivery schedule prescribed by him would have been an exercise in futility....

Id.

With respect to the second ruling, the Court of Claims noted that "[p]laintiff's actions, before [the Government's request for a new schedule], indicate a pattern of nonperformance and delay which should not be ignored. Although not justifications for default in themselves, they provide a context for understanding and evaluating plaintiff's continued problems." *Id.*

The Federal Circuit cited *Universal Fiberglass* with approval in the remand, which rejected the impossibility or abandonment requirement to sustain a default termination for failure to make progress. *See McDonnell Douglas,* 323 F.3d at 1015 (Termination for default for failure to make progress affirmed "despite lack of express repudiation") (citing *Universal Fiberglass,* 537 F.2d at 398). *Universal* also shows that an enforceable schedule is not necessary to determine whether performance is endangered in a failure to make progress case.

Universal holds that a schedule is not necessary because the cure notice supplants the schedule and serves a similar function. The cure notice lets a contractor know that even if performance or delivery is not yet due, the contracting officer believes the contractor may not be making sufficient progress to complete the contract on time. The burden is then on the contractor to advise the Government how it will

complete the project on time, according to contract requirements.

The Government did not waive its right to terminate the contractors for default by not reissuing a contract schedule for completion of the A-12. *Universal Fiberglass* holds the Government may call time on a contractor for failing to make sufficient progress without having reissued such a schedule. The Court of Claims' ruling eliminated the need for a schedule in a case such as this one, where the Government issued a notice to cure to alert plaintiffs to their deadline for making adequate assurances. *Universal Fiberglass* showed that default for failure to make progress may be appropriate well before the work is to be completed even in the absence of such a schedule because of the cure notice.

Universal Fiberglass highlights the importance of differentiating between failure to make progress and failure to deliver. In this case, plaintiffs were terminated for default nearly a year before performance was due. The issues in this case are layered and subtle compared to those of *Universal*.[63] Nevertheless, *Universal* suggests that the contractor defense of waiver as established in *De Vito* is inapplicable in

[63] The *Universal* court notes that "[p]laintiff was making no progress at all, had never manufactured a vehicle under the new specifications it had agreed to, did not have the necessary parts and could not obtain them and had allowed its labor force to wither away." *Universal Fiberglass*, 537 F.2d at 398. Moreover, the Government had already asked plaintiff for a new schedule and had been rebuffed. "If this situation is not what this failure to make progress clause is about ... we are at a loss to understand why it was put in the contract at all." *Id.*

this failure to make progress case. Though the contract may have not had a clear completion date, plaintiffs remained bound by their contractual duty to make progress.

The default clause for failure to make progress does not make reference to a schedule, but allows termination where a contractor is failing to make progress or to prosecute the work "so as to endanger performance." FAR 52.249-9. The question becomes, how would the Government know reasonably whether contract performance was endangered without a contract schedule. *See McDonnell Douglas,* 182 F.3d at 1332 ("Having determined that Contractors were obligated to make enough progress such that contract performance was not endangered, we must now address what progress Contractors should have made...."). Similarly, how might this court "decide ... the amount of time remaining for performance" to analyze whether the contracting officer had a reasonable belief there was no reasonable likelihood of timely completion. *McDonnell Douglas,* 323 F.3d at 1017.

Establishing a new enforceable schedule might be the easiest means to determine whether performance has been endangered, but according to *Universal* a schedule is not a precondition to termination. Nevertheless, the Government must have at least a "clear understanding of what needed to be done and how long it would reasonably take." *CJP Contractors v. United States,* 45 Fed. Cl. 343, 378 (1999). Use of this specified schedule of work and time is necessary to gauge the reasonableness of a termination for failure to make progress. Once a court has defined these

parameters, it may measure the contractors' progress in light of factors probative of plaintiffs' ability and willingness to perform.

D. THE YARDSTICK

The Federal Circuit implied in this case that a court may choose a reasonable period of performance to use as a measure of progress on the contract. *See McDonnell Douglas,* 182 F.3d at 1332 ("In litigation over a contractor's failure to make progress-unlike a dispute over failure to meet a specific contract requirement or schedule-courts must always determine *ex post* the threshold of performance that a contractor must meet to avoid endangering performance.") (citing Cibinic & Nash, *Administration of Government Contracts* 930-32). The phrase cited by the Federal Circuit in 1999, "courts must always determine *ex post* the threshold of performance that a contractor must meet to avoid endangering performance," suggests discretion in the trial court to define a yardstick that fairly measures the contractor's performance in the circumstances. The current remand order more clearly allows this: "[W]e leave it to the trial court to determine on first instance the actual performance required by the contract and the amount of time remaining for that performance." *McDonnell Douglas,* 323 F.3d at 1018.

The Federal Circuit ruled in 1999 that "[i]n the A-12 case ... there was a specified delivery schedule, including the delivery of the first FSED aircraft in December 1991." *McDonnell Douglas,* 182 F.3d at 1332 (citing the record for the original schedule for the eight FSED aircraft and the revised delivery

schedule for the same). The Circuit then noted that the A-12 contract "[t]herefore ... imposed a duty on contractors to make such progress so as not to endanger performance...." *Id.* The court of appeals held that "the contract, throughout its term, embodied a duty to make progress toward the ultimate end item" even though at termination the contract did not "embody [ ] the ultimate end item." *Id.*

The "actual performance required by the contract and the amount of time remaining for that performance" at termination may be a measure such as the yardstick discussed here. The Federal Circuit opened the door to P00046 or an alternative contract schedule for that purpose. It meets the Circuit's requirement that the court "decide the actual performance that the contract requires and the amount of time remaining for performance," *McDonnell Douglas,* 323 F.3d at 1016 (citation omitted), in absence of the ultimate contract closing date. The P00046 yardstick uses a contract period before the ultimate completion date for measuring performance, but one that encompasses more data for evaluation than a mere milestone. P00046 comprises a series of milestones, each with its own date due and its own standards of completion. The yardstick shows the contractors were behind schedule at termination according to a self-contained series of milestones, not in relation to the entire contract.

The P00046 schedule contained benchmarks for performance and delivery dates that were enforceable and explicit at termination. *See McDonnell Douglas,* 323 F.3d at 1019 ("Based on the information available at the time, the government's unilat-

eral schedule was reasonable."). One benefit of P00046 is that aircraft number eight has a definite date for delivery, not encumbered by a "sliding scale" of time resulting from references to other dates for calculation. For the purposes of measurement, this schedule represents the "entire contract effort."

The parties recognized before termination that the schedule against which the contractors were attempting to make progress was the P00046 delivery schedule. The Navy's purpose in issuing the partial contract modification was to allow the contractors to continue performing under the FSED contract despite their non-delivery on the first flight deadline in June 1990. Lot I was not a realistic concern for the Government during the months leading to termination. The Navy believed contract dates would be restructured eventually, or the contract would be cancelled. According to Captain Elberfeld, the Navy had "no Schedule for the Lot I aircraft that you would call a realistic schedule."[64] We use FSED aircraft numbers one through eight because realistically, they represent the performance "in play" at termination.[65]

[64] We do not reach the issue of whether the contractors could have been terminated for failure to make progress toward their Lot I obligations under the contract. Captain Elberfeld and the contractors point out that if all of the contract dates were in effect and enforceable simultaneously, the result would have been a nonsensical, overlapping schedule against which plaintiff could not realistically perform. It would have been impossible for the contractors to deliver Lot I aircraft on the dates the parties originally intended.

[65] Captain Elberfeld testified in 2001:

The severable nature of the A-12 contract assists the analysis. That is, the FSED portion of the contract was treated by the parties differently from the production phase, as separate contracts. The Lot I phase was added when the Navy exercised its first production option. Other contractors could have produced hundreds of A-12 aircraft once General Dynamics and McDonnell Douglas completed the research and development phase.[66] Also, the A-12 contract applied different FAR provisions to the FSED and production phases.

The separate FAR default clauses applied to each are significant for our purposes. FAR 52.249-9 authorizing termination for failure to make progress-the provision interpreted by *Lisbon*-applied only to FSED work under the contract. The Production Lots were to be governed by FAR 49.249-8.

P00046 provides an appropriate and "relevant" time period the court may use to consider whether

> The schedule for completing contracts is something that takes sometimes years. Some contracts [take] 10, 15 years before they're closed out, even after the last aircraft is delivered. So asking the schedule to close out contracts is-I don't know what the schedule is to close out the contracts. We had schedules for delivering aircraft, we had schedules for other milestones, like critical design review, preliminary design review, on the major program milestones. But I don't recall the contract saying and the contract will be completed and closed out on this date, as one of the requirements of the contract.

[66] The Navy asked bidders to form teams partly so the winning contractors could compete against each other for future production contracts.

the contracting officer could reasonably have been insecure about the contractors' rate of progress. In the Federal Circuit's terms, this permits the court to "determine[ ] the performance required by the contract and the contract completion date...." *McDonnell Douglas* at 1018.

Having determined P00046 defines "the performance required by the contract" and "the time remaining for contract performance," the next step is to "decide, in light of the information upon which the contracting officer relied" whether he had a reasonable belief that plaintiffs would not perform. *Id.* That is, whether he was "right," objectively.[67] As the court of appeals noted, "this is a determination ... on which [the Circuit] neither express[es] nor intimate[s] any view." *Id.* at 1018.

We "must take into account *all of the relevant facts and testimony*" in deciding whether default termination was justified. *Id.* at 1013 (emphasis added); *see also Id.* at 1017 ("The government owes the contractor no less than an assessment of all of the relevant circumstances when it exercises its discretion under the default clause.") (citing *Appeal of L & H Constr. Co.,* ASBCA No. 43,833, 97-1 BCA ¶ 28,766, 1997 WL 49588 (Feb. 5, 1997)). "In determining whether a default termination was justified, [trial] court[s] must review the evidence and circum-

[67] The law does not necessarily require that Admiral Morris or any contracting officer be right. The issue is whether "the Government" had in its possession sufficient information that would have justified the contracting officer's nominal concern had it been known. *See infra* note 69.

stances surrounding the termination, and that assessment involves a consideration of factual and evidentiary issues." *Id.* at 1014.

E. RELEVANT FACTS AND TESTIMONY

"'[R]elevant facts and testimony' include Contractors' statements that they could not meet the contract specifications, the contract delivery schedule, nor complete performance at the specified contract price."[68] *Id.* at 1013. We also consider other "tangible, direct evidence reflecting the impairment of timely completion" in deciding whether the contracting officer acted reasonably, *Id.* at 1016, including:

> [T]he contracting officer's testimony and contemporaneous documents. *Id.* at 1016 (citing *Lisbon*, 828 F.2d at 766);
>
> [T]he contractor's failure to meet progress milestones. *Id.* at 1017 (citing *James E. Kennedy, Jr. v. United States*, 164 Ct. Cl. 507, 512[, 1964 WL 8588] (1964); *Appeals of AAR Corp.*, ASBCA Nos. 16486, 16992, 74-2 BCA ¶ 10,653[, 1974 WL 2013] (Apr. 24, 1974));

[68] The Federal Circuit included these items in the remand order, knowing that they were the primary criticisms against plaintiffs on appeal. *Id.* at 1013. The Circuit's choice of these alleged shortcomings seemed to equate plaintiffs' failure to meet the schedule, their requests for more money, and their problems with some specifications, with legitimate bases for termination.

> [T]he contractor's financial situation. *Id.* (citing Universal Fiberglass, 537 F.2d at 395-96); and
>
> [T]he over-all evidence of [the contractors'] failure to prosecute diligently [their] work under the contract. *Id.* (quoting *Discount*, 554 F.2d at 441).

1. Contractors' Statements

"Contractors' statements that they could not meet the contract specifications, the contract delivery schedule, nor complete performance at the specified contract price" are relevant to deciding whether the termination for default was justified. *McDonnell Douglas,* 323 F.3d at 1016; *McDonnell Douglas,* 182 F.3d at 1332. The trial record supplies reasons that a contracting officer might have deemed himself insecure if he were considering the period of performance identified as the "yardstick." For example, plaintiffs' internal schedules showed they would not complete the prototypes covered by P00046 by February 1993. Mr. Anders, General Dynamics' CEO, commented in response to a question from Under Secretary Yockey that the plane would not "fly by 2 January [1991]. All deficiencies cannot be corrected. Can we deliver a satisfactory aircraft for the Navy? Mother Nature won't allow correction of all defects."

McDonnell Douglas' CEO, John McDonnell, said in the same meeting that the contract "has got to get reformed to a cost-type contract or *we cannot do it.* We need some form of Public Law 85-804." (emphasis added). Mr. Lamers, General Dynamics' Program

Manager during most of contract performance, agreed that restructure would be necessary.

Six months prior to termination, the contractors projected a twelve to fourteen-month delay in first flight [June-August 1991]. By termination, the contractors' expectations extended first flight to March 1992. TECHEVAL would be in July 1995. Plaintiffs could not meet their own schedule, or their representations regarding schedule. This fact is relevant to the issue of whether the contracting officer could have been concerned whether plaintiffs were making sufficient progress.

Neither contractor would commit to a bilateral schedule without first reaching agreement with the Government regarding outstanding "technical and business" issues. The parties were negotiating solutions to severe schedule slippage at termination. CEO Anders conceded plaintiffs would "do the best we can, and the Navy has to decide if that's good enough." General Dynamics' chief executive officer Pace said the contractors had "major financial problems." To support their request for an equitable restructuring of the contract, Mr. Pace sought to remove "financial strains upon the contractors that might prevent achievement of technical resolution." The parties' A-12 program manager, John Lamers acknowledged that "[s]ome kind of restructure would have to be accomplished if we were to get that aircraft into the fleet."

The contractors' admissions of inability to complete the work according to the P00046 schedule, alleged impossibility of satisfying the design require-

ments, and concerns about the business issues do not alone satisfy the Government's obligation to prove default. *McDonnell Douglas,* 323 F.3d at 1015. Such admissions may be sufficient in combination with other factors, however, to show that the contracting officer might reasonably have felt insecure. *See Id.* at 1016-17; *McDonnell Douglas,* 182 F.3d at 1328 ("The cost to complete a contract-more particularly, the inability of a contractor to perform a contract at the specified contract price are both fundamental elements of government contracts and are related to contract performance; as such, they are highly relevant to the question of default."). Among the other factors are the contracting officer's testimony and contemporaneous documents.

2. Contracting Officer's Testimony

"The Contracting Officer's testimony and contemporaneous documents are relevant" when deciding whether the default termination was justified. *McDonnell Douglas,* 323 F.3d at 1016.[69] The termi-

[69] The role of the contracting officer in deciding to terminate for default was another issue. The contractors contend the Government cannot sustain its burden because the contracting officer did not perform a *Lisbon* analysis, citing the Federal Circuit's remand order:

> Unless the contracting officer had determined the entire effort required under the contract and the time left to complete the contract, it would be difficult, if not impossible, for him to resolve whether there was no reasonable likelihood that the contractor could perform the *entire contract effort within the time remaining for performance.*

McDonnell Douglas, 323 F.3d at 1017 (internal quotation marks and citation omitted).

This statement is unclear in context. It does appear to lend support for the contractors' contention. The statement is not easily reconciled with the requirement that this court conduct a *de novo* review of the contracting officer's default termination decision. *Id.* at 1018 n.3. Factual findings show that Admiral Morris did not calculate a percentage of completion or consider all the circumstances.

The contractor in *Empire Energy v. Roche* argued that *McDonnell Douglas* adopted a special rule for terminations for failure to make progress that departed from the objective analysis requirement. 362 F.3d at 1357. The contractor claimed that "the contracting officer could not properly have terminated for failure to make progress because she [the CO] did not specifically consider whether [the contractor] could have completed the project within the period of excusable delay." *Id.* The Circuit reasoned:

> We have expressly held that the government must show in termination for failure to make progress cases that it was reasonable for the [government] to conclude that [the contractor] would be unable to complete the project by what the [reviewing court or] Board found to be the proper completion date.... *McDonnell Douglas* is not to the contrary. Indeed, *McDonnell Douglas* demands an objective inquiry, not an evaluation of the contracting officer's subjective beliefs.... It requires the court to consider whether the contracting officer's decision to terminate for failure to make progress was reasonable given the events that occurred before the termination decision was made.

Id. at 1357-58 (internal citations and quotation marks omitted). The court did not discuss further the excerpt

nation notice to the contractors stated that termination was "based on the Team's inability to complete the design, development, fabrication, assembly and test of the A-12 aircraft within the contract schedule and the Team's inability to deliver an aircraft that meets contract requirements." Testimony by Morris at trial supports these conclusions.

Admiral Morris expressed some reservations about contract completion during his testimony at the 1993 and 2001 trials. As the end of 1990 approached,[70] he was concerned that substantial development on the aircraft had yet to occur. He testified "[t]he contractors were indicating that they were experiencing an overrun that they could not absorb. Cost was obviously a factor and their failure to fabricate components, their failure to meet schedule were clearly impacting cost."

Admiral Morris explained that the contractors' "failure to fabricate parts was endangering performance because ... I didn't know at that particular time when in fact they would be able, if ever, to achieve [performance of the contract] ... and I was hearing 'we will not' or 'we could not' ..." Admiral Morris did not know when the contractors would finish, he said, if ever. However, he did not calculate the contractors'

cited above, but *Empire* clarifies the fact that Admiral Morris did not perform a *Lisbon* analysis is not dispositive.

[70] Admiral Morris testified that concerns about the A-12 Program "started arising very rapidly.... Those concerns increased, [he] belie[ved] the risks increased, as we got into the Fall of 1990."

percentage of completion or consider the FAR factors prior to termination. *See supra* notes 42-44 and accompanying text.

The contracting officer testified that in the weeks leading to termination, the contractors

> acknowledged they would not be able to achieve the contract specifications and the contract requirements.... [T]hey indicated that they would not be able to meet the delivery schedule that was currently in the contract. And ... they would not be able to perform the contract without extraordinary relief or additional funding for the contract.

Admiral Morris thought the contractors had not provided him sufficient information about cost or schedule. He quoted the contractors as informing him, in his words, "I don't know what I can provide, when I can provide it, and I can't tell you how much it's going to cost." The contracting officer summarized, "they basically said they can't perform under the contract and they were in default of it."

Admiral Morris did not commit such concerns to writing as they arose.[71] He encouraged the contractors to continue performing in the face of their al-

[71] Comments to plaintiffs from the contracting officer who preceded Admiral Morris, Mr. Michael Mutty, were an exception. Mutty wrote a letter to the contractors on July 12, 1990, after they did not delivery first flight on time. The letter stated they "failed to deliver the first aircraft as required by the contract. This failure could jeopardize performance of the entire FSED effort." *See infra* p. 429.

leged default.[72] Admiral Morris did not think the contractors' inability to complete performance on time was fatal to the contract, or to the Program. He wanted a finished product when he could get it.[73]

The Government cites the termination memorandum as a "contemporaneous memorialization" of Admiral Morris' belief that the contractors were in default at termination. A termination memorandum is an in-house document that provides evidence of the contracting officer's reasoning for the decision to

[72] Earlier factual findings by this court establish that Admiral Morris did not determine the entire effort required and the time left to complete that contract effort prior to termination. *See, e.g.*,35 Fed. Cl. at 364 n.6 ("[Admiral Morris] did not know the details of contract performance or the details of the contract specifications."); *Id.* at 367-68 ("Morris did not review any A-12 contract documents in preparation for the termination.... He did not review documents related to schedule or specifications."); *Id.* at 368 ("Admiral Morris testified at trial ... [that] under [Yockey's] guidelines, [he] couldn't do the one thing that [he] wanted to do, ... and that was continue the contract ...."); *see also supra* note 40. An analysis of Admiral Morris' testimony next to his conduct at the time shows that Admiral Morris was not concerned about the contractors' impairment of timely completion, but only wanted an eventual product for the Fleet.

[73] Admiral Morris was among the A-12's most enthusiastic cheerleaders before he was directed to terminate the contract, and after. Admiral Morris' testimony suggests that he worried about whether the contractors would complete the A-12 project. At termination, however, he was not particularly concerned about deficiencies such as failure to meet the delivery schedule; he did not think they were fatal to the A-12 Program. Admiral Morris' conduct throughout contract performance shows that he acknowledged the risk and the problems with performance, but he continued to encourage the contractors. *See McDonnell Douglas*, 35 Fed. Cl. at 366-67.

terminate. We disregarded the memorandum as evidence of the truth of its contents because of the circumstances surrounding its creation. For example, the Government maintains that the memorandum highlighted the "importance of [the contractors' purported two-year] delay" as a basis to terminate for default. The termination memorandum states in the conclusion, "[a]s a consequence of the team's delay, the Navy would be required to purchase production aircraft before verifying that the aircraft are operationally suitable and effective." Defendant cited this as support for its argument that the contracting officer's termination for default was reasonable. Admiral Morris did not reach such a conclusion regarding a two-year delay. Testimony during trial about a two-year delay apparently was meant to coincide with and offer support for the termination memorandum, though its source was an unrelated, land-based aircraft that Lockheed had attempted to build.[74]

Admiral Morris did not testify that he made such a determination or had such a concern. Indeed, he could not have. The A-12 contract schedule obligated the Navy to exercise its options to purchase the production lots before completion of the testing phases irrespective of contractor delay. Eleanor Spector testified that this element of the contract schedule was a risk known before contract award, not "a conse-

[74] The language quoted in the termination memorandum was taken from a termination memorandum used for another project, the P-7. Ms. Olsen had little time to craft a memorandum specific to the A-12 that busy Monday morning, January 7, 1991; this was the day the Government's half-billion dollar advance to plaintiffs was due. *See supra* pp. 409-11.

quence of the team's delay." The Navy had exercised the option to order six production aircraft, Lot I, in May 1990, before the original first flight deadline the following month.

The only section of the A-12 termination memorandum that addressed the program's schedule "stops short of a prediction." *McDonnell Douglas*, 35 Fed. Cl. at 367 n.12. Ms. Olsen and Admiral Morris neglected to fill in the blank provided by the P-7 memorandum: "Since June 1990, the team has consistently reported its delays; and the Navy's independent review confirmed that, given the state of the team's development efforts, delivery of aircraft and completion of related contract requirements could occur no sooner than ." [*sic*] This confirms that Admiral Morris did not conduct an analysis of the time it would likely take the contractors to complete the entire effort. Asked about this key omission during trial, Admiral Morris admitted, "obviously I blew it."

Admiral Morris wanted the opportunity to resolve the issues without extraordinary relief. At trial, he agreed that the contractors were in default and he testified he thought they should be terminated for default. The Federal Circuit interpreted this testimony as evidence plaintiffs were seriously in default at termination. *See McDonnell Douglas*, 182 F.3d at 1327 ("[T]he trial court's finding that the Navy went to great lengths to preserve the A-12 program suggests that it would not have terminated the contract

but for its belief that Contractors had breached the contract or would not perform the contract.").[75]

The contracting officer's testimony and contemporaneous documents do not provide sufficient evidence to prove justifiable termination for default. Admiral Morris' beliefs are not conclusive, however, but only a factor to consider upon review. *See McDonnell Douglas,* 323 F.3d at 1016 (holding "a court's review of default justification does not turn on the contracting officer's subjective beliefs but rather requires an objective inquiry."). "[We] may also consider other factors usually relied upon by courts and contract boards, such as .... the contractor's failure to meet progress milestones." *Id.*

3. Failure to Meet Milestones

The Federal Circuit ruled that concern about plaintiffs' missing a milestone is not a proper basis for termination. *Id.* at 1015 (citing *Lisbon,* 828 F.2d at 765). However, missed milestones may be considered in conjunction with other contractor shortcomings in determining whether the contracting officer

[75] Admiral Morris did not want to terminate the contract; he wanted the opportunity to continue despite the concern he expressed at trial that plaintiffs were in default. He would have attempted to work with the contractors even without a "bail-out" or other relief. Given his testimony during trial and contemporaneous records, the Government's insistence that he believed the contractors were seriously in default at termination seemed to put Admiral Morris in an odd position. The Circuit noted, however, that the Navy's and Admiral Morris' desire to continue the contract "does not thereby waive [the Government's] right to terminate for default." *McDonnell Douglas,* 182 F.3d at 1327.

made a reasonable decision to terminate for default. *Id.* at 1016-17.

The contractors did not deliver the June 1990 first flight on time according to the original schedule. They would not have delivered first flight on the revised schedule either. Missing a milestone could cause delay in the "building block" sequence of construction, irrespective of findings that the contractors were using their best efforts to improve and advance the project. Defendant points out that the contractors had missed several milestones by termination in December 1990-January 1991. CDR was scheduled to be completed by July 1989 (CLIN 0003). In 1989, the CDR was divided into a four-phase process. The third phase was still open at termination, and the fourth would not be completed until July 1991.

The contractors missed delivery of two prototypes before the Navy issued P00046, the modified contract schedule. The contractors admitted they would not meet various milestones in the future. Plaintiffs claim that no missed milestones were outstanding as of termination because first flight and the CDR milestones were waived through contract modifications. They contend that missed milestones have no legal significance in any event, because the contract had no binding completion date.[76]

The Navy did not terminate the contract when it became apparent CDR would not be completed on

[76] This is one indication of the importance of their interpretation of the remand order to the contractors; it has wide implications.

time; nor did it terminate when plaintiffs missed the original first flight date. Missed milestones do not necessarily give the Navy such authority. *See Ubique, Ltd.*, DOTCAB Nos. 71-28, 71-28A, 72-1 BCA ¶ 9,340, 1972 WL 1084 (Feb. 16, 1972) (Where the date contractor was due to present prototype for government inspection passed without delivery, "the Government could not have summarily terminated [contractor] for default").[77] Missed milestone dates may, however, be relevant. *See Universal Fiberglass*, 537 F.2d at 397 (Missed milestones "indicate a pattern of nonperformance and delay which should not be ignored. Although not justifications for default in themselves, they provide a context for understanding and evaluating plaintiff's continued problems"). Such information should be relevant if we consider whether a reasonable contracting officer might reasonably have been concerned about plaintiffs' ability to complete the contract on time.

4. The Contractors' Financial Situation

The contractors' financial situation, "particularly, the inability of a contractor to perform a contract at the specified contract price" is relevant to the question of default. *McDonnell Douglas*, 323 F.3d at 1017; *McDonnell Douglas*, 182 F.3d at 1328. We ruled in 2001 that "[n]either the cure notice nor the default notice suggests that the Navy thought the contrac-

[77] Perhaps the Government could not have terminated the contractors for failure to perform the work under the contract within the time specified, or any extension, *see* FAR 52.249-9(a)(1)(i), but not for an alleged progress failure that requires proof of "endanger[ed] performance." FAR 52.249-9(a)(1)(ii).

tors were financially unable to complete the contract" and that "plaintiffs' financial condition was not endangering performance of the A-12 contract." *McDonnell Douglas*, 50 Fed. Cl. at 320-21. The Government did not terminate plaintiffs for default on that basis. *Id.* Notwithstanding these conclusions, we may consider the contractors' financial situation as part of the over-all reasonableness inquiry mandated by the appeals court.[78]

Government officials close to the contract, including the Secretary of Defense, believed P.L. 85-804 was necessary to go forward with the A-12. This would permit a contract restructure or a "bailout," if needed. Morris did not close the door to negotiating a new contract without it, but he became more pessimistic after the notice to cure. He encouraged plaintiffs to address the cost overrun situation in response to the notice. He felt cost was a "real issue." Ms. Spector's testimony showed she agreed with Admiral Morris: "[W]hen a contractor has financial problems it's unable to do work-arounds. It's unable to do new technical approaches that may be necessary to solve a problem."

The contractors' requests for restructure of the A-12 contract are relevant too. The contractors ex-

[78] The Federal Circuit discussed the issue of financial ability in the remand after acknowledging that this court "declined to base its determination of justified default on Contractors' alleged financial inability to perform the contract." *McDonnell Douglas*, 323 F.3d at 1011. It is unlikely the appeals court would have directed consideration of plaintiffs' financial ability if that factor could not be a part of the "tangible, direct evidence" to which we should refer on remand.

pressed to the Navy in the Summer of 1990 and several times later that Fall their belief that insufficient funds were obligated to perform. Mr. McDonnell lamented: "The fixed-price nature of the contract precluded good management." He claimed that the A-12 contract "has got to get reformed to a cost-type contract or we cannot do it."

The Government did not terminate for default because of plaintiffs' cash flow problems. *McDonnell Douglas,* 50 Fed. Cl. at 320-21. Admiral Morris acknowledged he was not in a position to make decisions about contractors' financial position. *Id.* The contractors' requests to restructure the contract were not declarations of financial inability or unwillingness to perform. *Id.* However, evidence regarding how perceived financial problems may affect performance on the contract, such as statements by Admiral Morris, Ms. Spector, and Mr. McDonnell, are "highly relevant to the question of default." *McDonnell Douglas,* 182 F.3d at 1328. Representations of the contractors' grave financial position from parties close to the contract in the months prior to termination, support a finding of justifiable default measured by the P00046 schedule.

5. The Contractors' Failure to Prosecute

We may consider "over-all evidence of [the contractors'] failure to prosecute diligently its work under the contract." *McDonnell Douglas,* 323 F.3d at 1017 (quoting *Discount,* 554 F.2d at 441). This category goes to the merits of plaintiffs' performance, and it serves as a summary of matters discussed earlier.

The contractors' history of performance in general can be said to have involved delays and unresolved issues. Plaintiffs experienced a number of delays and problems with technical issues throughout contract performance.[79] Admiral Lockard emphasized that plaintiffs were having serious difficulties manufacturing aircraft parts. Contractors admitted after the June 1990 first flight date passed without delivery that they were experiencing a twelve to fourteen-month delay. TECHEVAL was scheduled to occur at least eighteen months after the April 1993 date in the original contract. The contractors acknowledged that all delivery dates in the Master Program Schedule would be delayed.[80] The contractors had not delivered two aircraft on time when the Navy unilaterally modified the delivery schedule in August 1990.

Despite delays, the contractors continued operations. They were spending $120 to $150 million of their own money every month. They were committed to performing the A-12 contract until the date of termination. The contractors were encouraged to spend their own money in part by the Navy's A-12 Program Review that found "[n]o major 'showstopper' technical issues." At termination, the Navy noted "a

[79] The nature of research and development contracts is such that most of the work normally happens during earlier periods of performance than is typical of construction or delivery contracts.

[80] This evidence shows that the contractors recognized performance problems during development of the A-12. The Master Program Schedule, however, has little meaning otherwise, because it includes only the original contract dates. These were not enforceable at termination.

modest uncertainty in first flight date," but also asserted that "system performance is good with excellent overall operational capability." The Navy acknowledged contractor delays but encouraged the contractors to continue. The Navy elected to go forward during the Design Review Boards with knowledge that the A-12 aircraft would not meet all specifications in the original contract. The contractors' strict conformance with each specification was not a principal concern of the Government's then. Some specifications were "chinning bars," set high to insure that the Navy would get the best aircraft possible.[81]

Plaintiffs did not intend to abandon the project, though a showing of abandonment is not necessary to establish failure to make progress. *See McDonnell Douglas,* 323 F.3d at 1015. Mr. McDonnell testified that "[t]he U.S. Navy was our biggest and most important customer. This was the program of the future for the U.S. Navy.... And so the biggest program for the longest future and our biggest customer, you don't stop performing on something like that."[82]

[81] The Navy may have been unsure what to include as performance specifications in the A-12 contract at the outset. This would be understandable, as no one had designed a stealth fighter that would land on an aircraft carrier.

[82] Trial notes confirm that this testimony, which otherwise may strike a finder of fact as self-serving, was entirely credible. Mr. McDonnell's testimony was honest and truthful with respect to his intentions and those of his company. Admiral Morris' contemporaneous impression of a January 1991 meeting with the CEOs was, "[b]oth companies committed." At the same meeting, he noted Under Secretary Yockey's agreement that the contractors were "mov[ing] in the right direction."

The test for reviewing the contracting officer's decision does not, however, include solely the effort expended by the contractors in attempting to meet the contract requirements. This court explained in a recent failure to make progress case that "[i]f that was our ultimate goal, the court would simply state that the record evidence establishes that [the contractors] worked very hard on the contract.... [Assessing whether the contractor failed to diligently prosecute the work] requires that we look at the results of the contractor's efforts...." *Aptus Co. v. United States,* 61 Fed. Cl. 638, 657-58 (2004), *aff'd sub nom. Lin v. United States,* 159 Fed. Appx. 186 (Fed. Cir. 2005), *cert. denied,*547 U.S. 1113, 126 S. Ct. 1921, 164 L. Ed. 2d 666 (2006).

Government officials decided uncertainty regarding schedule and cost was causing problems with continuing the Program. That is, the contractors' efforts were not "good enough." Government witnesses testified they believed plaintiffs were operating woefully behind schedule, and evidence supports their concern.

Admiral Lockard reported to Secretary Cann in September and November 1990 that he thought the contractors' progress was unsatisfactory. He testified about a "lingering technical concern" that first flight would be difficult to predict in early November 1990. He could not predict with accuracy when the first plane would fly until all the composite parts were successfully built, and getting those parts built created continuing difficulties. After a meeting of the Design Review Board for the third phase of CDR, he felt "hopeful" that he could declare CDR a success

and approve the A-12 design. He concluded "it was going to take a considerable amount of time for [the contractors] to figure out the problems that they were having [building composite parts repeatedly,] then correct everything to make it work."

Admiral Lockard explained: "I couldn't give my boss or anyone else a date we felt with certainty that we could stand up and say, they will be ready on this date."[83] Captain Elberfeld, Admiral Cook, Admiral Lockard, and Secretary Cheney all thought the contractors were in material breach.

Captain Elberfeld was concerned about the contractors' acknowledgment, beginning in Spring 1990, that they would be at or over the ceiling price. He thought this jeopardized the contractors' performance. The contractors' cash flow problems led to "cost cutting efforts like reducing staff, eliminating overtime, quick fixes that address and would remedy a cash flow situation." Captain Elberfeld learned in July 1990 that this meant removing 110 people from the A-12 program, which would result in more schedule problems. He said, it would cause "a longer process to get product that may not be the product that we desire or need."

Admiral Cook succeeded Captain Elberfeld as the A-12 Program Manager prior to termination. Admi-

[83] Admiral Lockard was the Chief Engineer of NAVAIR. He met with Admiral Morris near the end to discuss "the technical issues, could we get them resolved, if we could find a way to satisfy the business arrangements, to get the contractors to do the work.... We were unsuccessful in finding a way to get the contractors to do the work."

ral Cook had been "convinced ... [that] the program was not executable" by the first of the CDR Phases. Like Admiral Morris, he wanted a chance to continue building the A-12 because he thought it was "needed [for the Fleet]." However, he thought that a "bailout" was necessary for the contractors to be able to continue performing under the contract.

The concern among Navy officials throughout 1990 was first flight. They all knew the contractors would not meet the first flight milestones in June 1990 and December 1991, but it remained a troublesome issue because of the importance attached to this significant milestone. The following comments are taken from weeks of testimony and from a voluminous documentary record. They are necessarily selective, but they provide a flavor of the concerns that constitute evidence the Circuit discussed:

> Admiral Cook: The Navy would not "get eight FSED aircraft or anything of use ... without a bailout.... Period."

Admiral Lockard: Successful outcomes pursuant to the agreements reached at CDR were contingent upon resolution of outstanding business issues. Admiral Lockard testified that the contractors' failure make progress on the structural components-i.e., "big bones,"-was critical to the contract. He found that "[the contractors] were not making progress in building [the planes] ... they were severely behind ... and we couldn't assemble the first airplane until they were able to build these parts successfully." Admiral Lockard acknowledged that the contractor's difficulties in manufacturing parts did not suggest that

"they could never build the parts; I just thought that it was going to take a considerable amount of time for them to figure out the problems" and correct them. He believed the contractors could complete the contract, but that it would take longer than anticipated.

Admiral Morris was aware of Admiral Lockard's statement, "technical resolution on the airplane has been reached." He knew of Admiral Lockard's belief that the parties "were on the way to a satisfactory CDR conclusion [and] [t]he contingencies on the RFA close-outs are vital to the success of the program." Admiral Lockard also notified Admiral Morris that the contractors had not complied with the "contingencies," however. Secretary Cann, whom Admiral Lockard briefed regarding this noncompliance, responded that he was concerned about the contractors' management structure.

Captain Elberfeld: The contractors stated they would be "unthinkably" over the A-12 contract fixed-price ceiling; their internal "worst case estimate could bankrupt both corporations." The contractors' cost-cutting efforts to avoid bankruptcy "lead to more corner-cutting and more incomplete effort and basically a longer process to get a product that may not be the product that we desire or need for the Navy."

Eleanor Spector: The contractors were spending $120 to $150 million per month. Their next progress payment would be August 1991, and they could not sustain a negative cash flow, "particularly considering the drains on the programs." Public Law 85-804

was the only way to go forward; absent restructuring, the Navy would never receive a usable aircraft.

Michael Mutty, the contracting officer of the Naval Air Systems Command, testified that the contractors were not meeting their requirements under the A-12 contract. On July 12, 1990, Mutty sent a letter to the contractors expressing

> serious concern regarding [the contractors'] performance under the A-12 contract.... [Y]ou failed to deliver the first aircraft as required by the contract. This failure could jeopardize performance of the entire FSED effort. Neither in your letter nor afterward have you provided any basis on which I could conclude that any of your obligations under the contract should be excused.

This letter gave the contractors notice of the Navy's concern over their lack of progress, their failure to meet contract requirements, and their possible termination. If Admiral Morris did not communicate his unease over A-12 to plaintiffs, or commit it to writing, Mutty did. He conveyed to the contractors "serious concern" regarding timely contract completion.

The issue on remand is whether a reasonable contracting officer, basing his termination decision on tangible, direct evidence reflecting the impairment of timely completion, could reasonably have decided to terminate the contract for default. The Circuit described factors to consider in answering this question. These include the contracting officer's testimony and contemporaneous documents, the contrac-

tors' failure to meet progress milestones, the contractors' financial condition, and other pertinent circumstances surrounding the termination decision.

This Opinion includes mitigating factors for plaintiffs in the discussion above and throughout the Opinion, in an effort to give a true picture of the issues a finder of fact faces in this case. Additional such factors are explained below. Overall, however, evidence of record supports a conclusion that the Government was justified in terminating the contract for default for failure to make progress.

III. CONTRACTORS' DEFENSES

The Government found no reasonable likelihood that McDonnell Douglas and General Dynamics would complete their contract obligations within the specified contract time. The default termination must stand unless the contractors prove the default was unlawful or excused. The contractors have the burden of proving such defenses. *RFI Shield-Rooms,* ASBCA Nos. 17374, 17991, 77-2 BCA ¶ 12,714, 1977 WL 2320 (Aug. 11, 1977).

The contractors assert three interrelated defenses: (1) the Navy waived the A-12 contract delivery schedule; (2) if the original schedule was not waived, the P00046 modification created a nonsensical overlapping schedule to which the contractors could not be bound; and (3) the contract had no completion date for the "entire contract effort" at termination, leaving no possibility the contracting officer reasonably concluded the contractors would not complete the work on time. These are intertwined with

plaintiffs' arguments that the Government could not meet its burden under *Lisbon*.

A. WAIVER OF DELIVERY SCHEDULE

Plaintiffs maintain that defendant waived or "disestablished" the original schedule to completion when it allowed the contractors to continue working beyond the June 1990 delivery date, and reset only a part of the work required under the original contract. They cite the remand to support this contention. *See McDonnell Douglas*, 323 F.3d at 1019 (discussing *DeVito*, 413 F.2d at 1154-55). *DeVito* held that

> [w]here the Government elects to permit a delinquent contractor to continue performance past a due date, it surrenders its alternative and inconsistent right under the Default clause to terminate, assuming the contractor has not abandoned performance and a reasonable time has expired for a termination notice to be given. This is popularly if inaccurately referred to as a "waiver" of the right to terminate.... The necessary elements of an election by the non-defaulting party to waive default in delivery under a contract are (1) failure to terminate within a reasonable time after the default under circumstances indicating forbearance, and (2) reliance by the contractor on the failure to terminate and continued performance by him under the contract, with the Government's knowledge and implied or express consent.

413 F.2d at 1153-54.

Plaintiffs assert that the Government waived all dates in the original schedule by encouraging the contractors to continue work after they missed the June 1990 first flight deadline, and that the Government must reset the entire schedule in such circumstances to reestablish time of the essence.

Defendant's position is that *DeVito* addresses the Government's burden to reestablish missed delivery dates, but it does not require the Navy to reestablish dates that have not yet come to pass. It argues,

> [n]othing in the law forced the Navy to decide on July 1, 1990, whether to terminate the A-12 contract immediately, or grant plaintiffs a windfall of resetting the entire schedule in response to plaintiffs' being late on the first delivery.... Government contractors do not gain contractual leverage via their defaults.[84]

We agree. The effect of plaintiffs' argument is the Navy should anticipate the need for reestablishing new dates at least five years into the future, and we and do not view the *DeVito* waiver rule so broadly as plaintiffs claim. At most, the court of appeals' reference to *DeVito* meant that Government waived its right to terminate plaintiffs for missing the original first flight date in June 1990 by "permit[ting] [the] delinquent contractor[s] to continue performance

[84] This is a version of the strawman fallacy, but it shows why a definable and measurable schedule is the more reasonable and pragmatic means of resolving this issue.

past [this] due date." *McDonnell Douglas,* 323 F.3d at 1019.

A waiver generally is considered an intentional relinquishment of a legal right. A finding under *DeVito* that the Navy waived its right to terminate plaintiffs for default in this case would assume irrational behavior on the Navy's part.[85] That is, the Navy must have intentionally relinquished its right to enforce the entire schedule by issuing P00046, then chosen to reset only the missed delivery date and the remaining FSED dates. P00046 contains boilerplate language that may protect against such a result. Having stated new dates for the eight aircraft, the modification stated, "all other terms and conditions of the contract remain unchanged."

A showing of detrimental reliance is necessary to prove waiver of a schedule. *DeVito,* 413 F.2d at 1154. We find no such prejudice to plaintiffs. On July 12, 1990, the contracting officer advised plaintiffs in writing that their failure to meet first flight "could jeopardize performance of the entire FSED effort." The Navy asked the contractors to submit plans to meet the schedule for the entire program. Plaintiffs did not respond. The Navy recommended a schedule that projected delay in all delivery dates, including an eighteen-month slip in TECHEVAL. Still, plaintiffs would not agree to a bilateral modification.

[85] We do not overlook the possibility that the Navy, like many contractors, could have fallen into a trap for the unwary and suffered unintended consequences. Contractors are presumed to know and understand the court-driven complexities of their actions during contract performance; the Government should be equipped to accept those risks as well.

Plaintiffs were well aware then that the Navy was concerned about schedule issues and that the entire program could be cancelled by the Department of Defense.

Most of the cases to which plaintiffs refer in support of the schedule waiver theory are factually and legally distinguishable. *See, e.g., SIPCO Servs. & Marine, Inc. v. United States,* 41 Fed. Cl. 196 (1998); *Robert E. Moore Constr.,* AGBCA No. 85-262-1, 90-2 BCA ¶ 22,803, 1990 WL 57479 (Apr. 25, 1990). In *SIPCO,* this court found the agency waived the contract completion date by allowing the contractor to continue deliveries, though deliveries were late. 41 Fed. Cl. at 211. Moreover, the court found that the Government's unilateral modification, which set a new contract completion date, was not "reasonable from the standpoint of the performance capabilities of the contractor." *Id.* In *Robert E. Moore,* the Government did not satisfy its burden of proving reasonableness of a new delivery date after it had waived an older date. 90-2 BCA at ¶ 22,803. The parties were therefore operating without a delivery date, thus the termination for default for failure to deliver was not justified. *Id.* These and similar board decisions are examples of a Government waiver after contractor default.

A reason it is difficult to apply such cases to this one is the important distinguishing factor in *DeVito* and other cases finding waiver-timing of the missed delivery date. In *DeVito,* the contractor missed the final delivery date; waiver occurred after the contractor delivery default. The Government waived an old delivery deadline by not issuing one, leaving the con-

tractor without notice of how much time was left for performance. Whether a notice to cure or a reestablished schedule of completion, these cases seem to address a similar commonsense requirement notice.

Plaintiffs' argument that the Government waived its right to terminate tends to contradict the law of this case. They have not addressed the Circuit's implied ruling that the Navy reestablished its right to terminate for default by issuing P00046. *See McDonnell Douglas,* 323 F.3d at 1019. If the court of appeals had found that the Navy waived the entire schedule, it would not have remanded the case for this court to "determine[ ] ... the contract completion date." *Id.* at 1018.

The effect of plaintiffs' waiver argument is that defendant's failure to establish an ultimate contract completion date disposes of the Government's right to terminate. Not having established or reset a schedule for the entire contract after the *DeVito* waiver in 1990, defendant could not use failure to make progress as an incidence of default during the contract's pendency. This would be a harsh result. More importantly, however, such an interpretation would neutralize the Circuit's discussion of "tangible, direct evidence" needed to consider whether termination was justified. *McDonnell Douglas,* 323 F.3d at 1017. We do not interpret the Circuit's remand or existing case law so strictly.

B. OVERLAPPING SCHEDULE

Plaintiffs assert that if the original delivery schedule to contract completion was not waived, the Navy's issuing P00046 created an overlapping

schedule impossible for the contractors to meet. Under the original schedule, the fourth aircraft of Lot I and modified first flight would apparently be due the same month, December 1991. *See supra* note 21.

The Government points to the Changes Clause of the contract, which requires plaintiffs to inform the Navy within twenty days of any actions or inactions they consider to be changes to the delivery schedule. Plaintiffs did not file such notifications. After plaintiffs missed the delivery date in June 1990, the Navy asked them to propose a new contract schedule. They refused, because for the contractors, "global issues" facing the A-12 program in mid-1990 took precedence. Plaintiffs did not want a binding schedule until these matters were resolved. According to defendant, plaintiffs therefore "acquiesced" in the continued enforceability of the original schedule.

The overlapping schedule offered by the Government as a basis for assessing default is unreasonable and likely unenforceable. The A-12 contract was designed as a long-term research and development effort, structured so that each period of performance built upon preceding work. Progress cannot be assessed in relation to milestones, but only in comparison to the entire contract effort. *See McDonnell Douglas,* 323 F.3d at 1016. The Government contends that the Lot I schedule remains in effect because that portion of the original contract was not changed by P00046.[86] In other words, the Lot I

[86] The P00046 modification does not have a milestone built in for completion of the contract or a date at when the fourteenth and final aircraft would be delivered. The modification addressed only the schedule for delivery and testing on the first

schedule remains in effect and plaintiffs would not make the deadlines provided there. This means production aircraft would be due before some of the prototypes. Application of the contract in that manner would be nonsensical.

Plaintiffs other argument on this issue is breach of contract. The contractors assert that defendant's argument regarding enforcement of the Lot I schedule as drafted breaches their contract right to a "sequential" delivery schedule. If the contract guaranteed plaintiffs a sequential schedule, however, P00046 itself would be unreasonable and unenforceable. Without the modification, the contract's sequential order would remain. Apparently, plaintiffs made a version of this argument to the Federal Circuit and it was rejected. The appeals court ruled that P00046 was reasonable and enforceable. *See Id.* at 1018-20.

The Navy probably could not have enforced the Lot I delivery dates, but it does not seem necessary to get that far into the analysis. The yardstick approach employs a schedule that we know to be reasonable and enforceable because the Circuit has so ruled-that is, P00046.

eight planes. Presumably, Lot I would have begun after the contractors delivered eight prototypes to the Navy's satisfaction. However, the schedule offered by the Government set delivery for the first FSED airframe in December 1991 and plane nine, the first aircraft in Lot I, remained due June 1991. Lot I would commence six months before the first test aircraft was to be delivered.

The *Lisbon* review takes a realistic look at the schedule that the parties were working toward at termination. Failure to make progress against an overlapping schedule would not be a reasonable basis for default. Not only would it be unfair, but also it would be inimical to the contract's purpose, to design, then manufacture and test successively more technically complex stealthy aircraft for the Navy's fleet. This is the main reason that we are left with the "yardstick approach."

C. CONTRACT COMPLETION DATE

This Opinion has addressed plaintiffs' arguments that the Navy waived the contract schedule and that the schedule was rendered "nonsensical" by the P00046 change order.[87] Plaintiffs offer the additional claim that the contract had no completion date for the "entire contract effort" at termination, leaving no possibility that the contracting officer reasonably concluded the contractors would not complete the work on time.

No one expected to enforce the Lot I schedule. Plaintiffs base their theory in part on this finding.

[87] The schedule for design, manufacture, testing, and production of the A-12 aircraft was to be performed in sequence. This is typical of research and development contracts, as compared to construction contracts or contracts calling for periodic delivery of identical end items. McDonnell Douglas' arguments assume that this sequential approach to performance was a contract requirement. *See McDonnell Douglas,* 35 Fed. Cl. at 362 (noting that "[e]ach FSED aircraft would test different characteristics of the A-12; stealth capabilities would be verified in the 'fully capable, fully equipped' eighth aircraft that would serve as the basis for the production lots.").

See McDonnell Douglas, 50 Fed. Cl. at 317-18 (citing Captain Elberfeld's testimony). If the Circuit had affirmed the ruling that P00046 was reasonable and enforceable because the entire contract had no schedule to completion, the appeals court would not have asked us in the same opinion to find a contract completion date. Captain Elberfeld's comments meant only that no one was considering Lot I or TECHEVAL, or any other dates at termination. Only P00046 was on the table. This court's review of "events, actions, and circumstances leading to termination" must exclude considerations of what might have been expected up to five years later.

The contract had no completion date at termination, seemingly leaving the court without a basis for finding a reasonable belief on the part of the contracting officer that the contractors would not complete the work on time. However, the appeals court did not rule that we should reject the *Lisbon* test if no contract completion date applies. The contractors acknowledge that such a reading is merely implicit in the remand decision. The Circuit was aware of both parties' interest in a contract completion date, which apparently was argued strenuously on appeal. The Federal Circuit did not suggest that *Lisbon* would not apply in such event, but explained repeatedly that the trial court should apply *Lisbon.*

Many cases to which plaintiffs refer are not helpful, given our facts. They involve the complete absence of any schedule for the contractual work.[88]

[88] *See Appeal of Lanzen Fabricating, Inc.,* ASBCA No. 40328, 93-3 BCA ¶ 26,079, 1993 WL 190380 (May 24, 1993) (Govern-

Plaintiffs also argue *Electronics of Austin,* a Board case similar to *McDonnell Douglas. See Appeal of Electronics of Austin,* ASBCA No. 24912, 86-3 BCA ¶ 19,307, 1986 WL 221174 (Aug. 14, 1986). In *Austin,* the Government had waived the performance schedule, and "there was no time frame within which [the plaintiff] had to perform." *Id.* For that reason, the Board found plaintiff could not be terminated for failing to make progress. The Federal Circuit distinguished *Austin* from this case because in *McDonnell Douglas,* the appeals court found a "specified delivery schedule." *See McDonnell Douglas,* 182 F.3d at 1332. The schedule "includ [ed] the delivery date of

ment's right to terminate for default may be defeated by government conduct after default "which either condones the default, or encourages or asks for continued performance, or fails to set a new delivery schedule"); *Appeal of M.V.I. Precision Machining, Ltd.,* ASBCA No. 37,393, 91-2 BCA ¶ 23,898, 1991 WL 46116 (Mar. 15, 1991) (default termination of supply and service contract overturned because the Government did not establish a "valid and subsisting delivery schedule" and the contractor therefore "could not be late in making delivery in accordance with ... [a] nonexistent schedule or in making progress under such [a] nonexistent schedule"); *Appeal of Motorola Computer Sys., Inc.,* ASBCA No. 26794, 87-3 BCA ¶ 20,032, 1987 WL 41115 (July 15, 1987) (default termination of supply and service contract reversed upon finding that "with no performance schedules in existence, in accordance with which [the contractor's] progress could be measured, the termination ... was improper") *Appeal of Humphrey Logging Co.,* AGBCA Nos. 85-203-3, 85-181-3, 84-359-3, 85-3 BCA ¶ 18,433, 1985 WL 16976 (Sept. 30, 1985) (default termination of construction contract overturned because the delivery schedule was waived and no schedule ever reestablished). Where the contract expires but the contractor continues to work with no new completion date to measure progress, a much simpler analysis presents itself.

the first FSED aircraft in December 1991.... Therefore, the [A-12] contract imposed a duty on Contractors to make such progress so as to not to not endanger performance." *Id.*

The Circuit ruled that plaintiffs had a duty to make progress because the contract contained "a specified delivery schedule, including the delivery of the first FSED aircraft in 1991." *Id.* This ruling supports the yardstick approach discussed above. If plaintiffs were obligated to make progress against the portion of the contract that was enforceable at the time, the P00046 modified schedule was an appropriate measure of that performance. *See McDonnell Douglas,* 182 F.3d at 1331-32 (ruling that plaintiffs were required to make progress toward an "ultimate end item" if not to contract conclusion, where funds had not been obligated to the entire contract).

IV. ADEQUATE ASSURANCES

The Government raises plaintiffs' lack of adequate assurances again, apparently on the basis that such a failure operates as an independent incident of default. That is, the contractors did not provide the Navy adequate assurances of timely performance in response to the cure notice. The judgment in this case moots defendant's alternative argument that plaintiffs did not provide adequate assurances to the contracting officer after receiving his notice to cure. This court's views on that issue have not changed. The findings of fact and conclusions of law related to adequate assurances are incorporated herein by ref-

erence. *See McDonnell Douglas,* 50 Fed. Cl. at 321-23.

Defendant believes the contractors' admission that they would not meet the delivery schedule or certain technical specifications required by the contract demonstrates lack of adequate assurances as a matter of law. We ruled in 1996 that the contractors did not repudiate the contract. *See McDonnell Douglas,* 35 Fed. Cl. at 377. The Government did not view the contractors' actions in this manner. *Id.* Admiral Morris did not believe that the contractors would not perform; he wanted an opportunity to work out the problems "within the boundaries of the contract." *Id.* n.31. Witnesses for the Government and for plaintiffs confirmed that the contractors intended to complete the contract.

A traditional repudiation claim required proof of a "positive, definite, unconditional, and unequivocal manifestation of intent ... not to render the promised performance when the time fixed ... by the contract shall arrive." *Id.* (quoting *Cascade Pac. Int'l v. United States,* 773 F.2d 287, 293 (Fed. Cir. 1985)). The Government points out that since the 1996 ruling, a new view of anticipatory repudiation has emerged. The modern rule acknowledges the Government's right to obtain assurances of timely performance in response to a justifiable cure notice and to declare the contractor in default for failure to provide such assurances. *See Danzig v. AEC Corp.,* 224 F.3d 1333 (Fed. Cir. 2000).

Danzig was an issue during the last trial. We discussed its application to this case at 50 Fed. Cl. at

321-23, pointing out that "[n]one of [*Danzig's*] facts is present here." *Id.* at 322. Pertinent excerpts from that discussion follow:

> In response to the cure notice issued by the Navy, the contractors stated that they were committed to the program and were providing a response to the concerns raised by Admiral Morris. The contractors addressed Admiral Morris' cure letter and provided additional information about the progress of the program. Certain specifications and delivery schedules would not be met, but the contractors explained why this was so. They alleged that certain requirements were impossible to satisfy, for example. Unlike AEC, McDonnell Douglas and General Dynamics continued to perform until they were terminated for default. They were spending between $120 and $150 million per month on the A-12 contract....

Admiral Morris did not view the contractors' response to the cure notice as failing to provide adequate assurances.

> The Government points to the contractors' request for equitable restructure of the A-12 contract as evidence that their financial situation would not permit the contractors to complete this contract. The proposal for restructure was not a response to the cure notice. It was a request for financial assistance. It was not included with the

> cure notice response but was a separate document with a separate cover sheet. Admiral Morris took notes at a January 2, 1991 meeting with the contractors. He records Mr. Anders, Chairman-Elect of General Dynamics, as stating, "[b]oth companies committed." [Under Secretary] Yockey agreed that contractors were "mov[ing] in the right direction." Failure to give adequate assurances does not appear in the termination notice as a ground for default. While the contractors wanted a restructured program they did not state they would suspend work on the A-12 contract. John McDonnell, CEO of McDonnell Douglas, testified that the contractors "weren't about to abandon [the A-12 contract]." Admiral Morris testified that he "would not have terminated the contract on the 7th of January if I got the authority to give it one more try."
>
> Plaintiffs did not repudiate this contract. Admiral Morris did not terminate the A-12 contract because the contractors did not give adequate assurances.

Id. at 322-23.

Following this court's ruling on adequate assurances, defendant raised the issue twice before the Federal Circuit. Defendant wrote:

> Government officials were entitled, as a matter of law, to rely upon the assurances of the contractors' most senior

> management that ....they would not perform the existing contract in determining whether the program should be continued, as well as whether the contractors were in default.... Indeed, the default may be sustained solely upon the basis of the contractors' anticipatory repudiation of the existing contract in their formal response to the cure notice.

Gov't Brief to Federal Circuit 40 (May 24, 2002). The Government also briefed this argument extensively in its petition for rehearing:

> The contractors' oral and written statements in the wake of the cure notice unambiguously gave the Government no "continuing sense of reliance and security that the promised performance ... [would] be forthcoming when due.... Given this, *AEC* requires, as a matter of law, that the judgment sustain the default be affirmed.... The Panel's failure to mention the substantive holding of *AEC* creates the impression that *AEC* may not present the law of the Circuit."

Gov't Combined Pet. for Rehearing and Rehearing *en banc* 5, 6-9 (June 16, 2003).

Defendant contends that the Federal Circuit vacated this court's rulings on the alternative basis that the contractors failed to provide adequate assurances. The 2003 opinion of the appeals court is best understood as leaving open the question of adequate assurances, the Government urges. The re-

mand order does not support such a conclusion. The appeals court gave no direction whether we must address defendant's alternative ground for default, yet it remanded the case to apply *Lisbon*. *See McDonnell Douglas*, 323 F.3d at 1024 ("[B]ecause the Court of Federal Claims did not apply the controlling standard under *Lisbon* to this case, we vacate its ruling that the default termination was justified and remand for further proceedings consistent with this opinion.").

The law of the case doctrine prevents further consideration of adequate assurances in these circumstances. *See, e.g., Am. Satellite Co. v. United States*, 34 Fed. Cl. 468, 480 (1995) ("It is well-settled that if the decision below is correct, 'it must be affirmed, although the lower court relied upon a wrong ground or gave a wrong reason.' ") (quoting *Helvering v. Gowran*, 302 U.S. 238, 245, 58 S. Ct. 154, 82 L. Ed. 224 (1937), *reh'g denied*,302 U.S. 781, 58 S. Ct. 478, 82 L. Ed. 603 (1938)). "If the Federal Circuit had accepted defendant's argument ... it would have affirmed this court's decision on other grounds; the remand order would have been moot. It is reasonable to assume that the Federal Circuit rejected the [argument]." *Am. Satellite*, 34 Fed. Cl. at 480.

Although the Federal Circuit's remand did not address specifically the adequate assurances argument of defendant, further consideration of the issue by this court is precluded by the Circuit's opinion. The Circuit would not have remanded the case for us to apply *Lisbon* if an alternative reason to sustain the default termination existed. Such a gesture would not have been useful.

We have no reason to evaluate the adequate assurances issue differently in any event. The factual findings upon which the earlier ruling depends have been affirmed, or they have not been called into question by the Federal Circuit. The Government has not offered evidence to cause us concern about the prior rulings on adequate assurances.

V. LOSS ADJUSTMENT

Federal Acquisition Regulations give the Government the right to a "credit" for losses the contractors would have incurred had the contractors performed to completion. *See* FAR 49.203; *McDonnell Douglas Corp. v. United States,* 37 Fed. Cl. 270 (1996) (explaining application of the loss adjustment clause). We held in 1996 that the loss adjustment issue was so intertwined with plaintiffs' arguments relating to superior knowledge and state secrets that neither that matter nor plaintiffs' claim for lost profits could be resolved safely. *Id.* at 272.

The Federal Circuit declined to address the merits of this issue in 1999, stating it was not yet ripe because the question of default remained unresolved. *McDonnell Douglas,* 182 F.3d at 1329-30. The Circuit vacated the rulings on plaintiffs' superior knowledge claim, as well as those for loss adjustment and profits, speculating that the passage of time may have lessened the risks involved. *Id.* at 1330;*see McDonnell Douglas,* 323 F.3d at 1013 (noting the Circuit's ruling vacating this court's loss ratio ruling on earlier appeal).

We readopted the loss adjustment ruling that this and other issues tied to plaintiffs' superior knowl-

edge claim could not be tried because the passage of time did not lessen threats to national security. *McDonnell Douglas Corp. v. United States,* No. 91-1204C (Mar. 1, 2001) ("All of the reasons established by [this court's] December 1996 opinion persist."). We denied the Government's motion for reconsideration in April. The default trial began later that spring.

The 2001 opinion following trial dismissed plaintiffs' superior knowledge claims upon finding that the Government properly invoked the state secrets doctrine. *McDonnell Douglas,* 50 Fed. Cl. at 324-25. We concluded that "[i]ssues involving superior knowledge cannot be litigated safely. Defendant's argument that it is entitled to a loss adjustment pursuant to FAR 49.203 and plaintiffs' lost profits argument are moot." *Id.* at 325.

The Circuit affirmed this court's rejection of the contractors' superior knowledge claim. Noting that the Government owes a duty to disclose certain "critical information" to a contractor, "well-established precedent demonstrates that, when a properly invoked claim of State Secrets privilege undercuts a civil litigant's opportunity to prove its case, the interests favoring the protection of the state secret always prevail." *McDonnell Douglas,* 323 F.3d at 1024. The Federal Circuit did not address loss adjustment arguments specifically. The Government contends this is so because we sustained the default, and defendant did not argue it on appeal.

Defendant asserts the court may enforce the A-12 contract's mandatory loss adjustment provision because it is no longer tied to superior knowledge. That

is, because we dismissed plaintiffs' superior knowledge defense, plaintiffs cannot rely on it to argue against this court's application of a loss adjustment. Plaintiffs lack a basis for invoking the doctrine as a defense to enforcement of the provision of the A-12 contract that mandates application of a loss adjustment.

These are reasonable arguments,[89] but they are legal arguments that we have no need to address at this stage given the judgment entered below. An adjustment under FAR presumes conversion to termination for convenience of the Government. Because we sustain the default termination under *Lisbon*, defendant's loss adjustment argument is moot.

CONCLUSION

This case demonstrates that the contracting officer may have a de minimis role in some circumstances of government procurement, rather than the central role that most contractors assume.[90] The contracting officer need not make termination decisions for the same reasons that a reviewing court may con-

[89] Attorneys for McDonnell Douglas, for General Dynamics, and for the United States have provided outstanding advocacy at the trial level through many years of difficult litigation. Their efforts have assisted the court immeasurably.

[90] Contractors are accustomed to regarding the role of a contracting officer as a central one under the Contract Disputes Act. For example, case law permits the Government to repudiate otherwise legitimate contracts because an official given apparent authority is not the contracting officer. Policy reasons for this practice may be clear, but it gives the contracting officer an exaggerated position in the experience of many contractors.

sider after termination.[91] So long as information to support the contracting officer's decision was available to the Government at termination, this is sufficient to rule whether the contracting officer reasonably terminated the contract for default for failure to make progress.

The parties had a mutual understanding that this contract would take many years to complete. It was an open-ended contract, as Captain Elberfeld explained: The "final act" of a research and development contract "depend[s] on what they were doing and what they were having problems accomplishing.... Until you get to the end, you don't know what the last step is." Yet the Government decided to ter-

[91] The Government need show only that a contracting officer acting reasonably with the benefit of information available to "the Government" at termination could have been justified in terminating the contractor for default. The information available to the Government need not have been known to the hypothetical contracting officer or, presumably, to the contractor, if a contracting officer could have found himself feeling insecure about contract completion as a result. He need not have included the reasons for his insecurity in the notice to cure or notice of termination. *See, e.g., Divecon Servs., LP v. Dep't of Commerce,* GSBCA No. 15997, 04-2 BCA ¶ 32,656, 2004 WL 1405648 (June 22, 2004) (holding "[w]hether a reason was cited by the contracting officer or even known to him at the time of termination is immaterial. If a valid basis for termination for default existed at that time, we will uphold the decision.") (citing *Empire,* 362 F.3d at 1357; *Kelso v. Kirk Bros. Mech. Contractors, Inc.,* 16 F.3d 1173, 1175 (Fed. Cir. 1994); *Joseph Morton Co. v. United States,* 757 F.2d 1273, 1277 (Fed. Cir. 1985); *Pots Unlimited, Ltd. v. United States,* 220 Ct. Cl. 405, 600 F.2d 790, 793 (1979); *ESC Polytech Consultants, Inc. v. Gen. Servs. Admin.,* GSBCA No. 12509, 95-2 BCA ¶ 27,629, 1995 WL 147423 (Mar. 31, 1995)).

minate this contract less than three years into performance.

The contractors had reason to expect the Government to approach this contract as it had before, and particularly as it has since. William Anders, General Dynamics' chief executive officer, commented, "[w]e jointly created a bad contract." We have a "mutually bad deal." Few would disagree with that judgment. Mr. Anders added, however, "[the] Government has a responsibility also to fix the contract."

The law does not require the Government to help "fix the contract." The Government can point to reasons in retrospect why plaintiffs were not making the progress that some officials hoped and perhaps expected. So long as those reasons form a rational basis for a reviewing court to uphold defendant's decision to terminate, the court must do so.[92]

Defendant's motion for judgment upon additional findings is GRANTED. Plaintiff's cross-motion is

[92] The reviewing court may decide whether a contracting officer's belief would be reasonable if it can "decide the actual performance that the contract requires and the amount of time remaining for performance." *McDonnell Douglas,* 323 F.3d at 1017 (citing *Lisbon,* 828 F.2d at 766). The case turns on whether the Circuit's remand meant for the clauses, "entire contract effort" and "contract completion date" to mean exactly what they appear to mean-the contractors' expansive view; or whether the remand permits our use of a more compact yardstick-coinciding with the Government's restricted view. The Government did not establish a contract closing date and the contracting officer did not conduct a *Lisbon* analysis prior to termination.

DENIED. All pending motions necessarily decided by this ruling are moot and therefore DENIED. The Clerk of Court will enter judgment for defendant. No costs.

APPENDIX C

United States Court of Appeals,
Federal Circuit.

McDONNELL DOUGLAS CORPORATION,
Plaintiff-Appellant,
and
General Dynamics Corporation,
Plaintiff-Appellant,
v.
UNITED STATES,
Defendant-Cross Appellant.

Nos. 02-5034, 02-5035, 02-5046.

March 17, 2003.
Rehearing and Rehearing En Banc Denied
Aug. 27, 2003.

Before MICHEL, CLEVENGER and LINN, Circuit Judges.

CLEVENGER, Circuit Judge.

This case arises from the government's default termination in 1991 of a contract between the United States Navy and defense contractors McDonnell Douglas Corporation and General Dynamics Corporation (the "Contractors") to develop a carrier-based stealth aircraft. The Contractors challenge the judgment of the Court of Federal Claims in favor of the government, *McDonnell Douglas Corp. v. United States,* 50 Fed. Cl. 311 (Fed. Cl. 2001) ("*McDonnell Douglas XI*"), and the government cross-appeals for

the return of unliquidated progress payments. Since the trial court misunderstood our mandate and misapplied the controlling standard, we vacate its judgment and remand. However, we see no error in the trial court's determination that the unilateral schedule imposed by the government was enforceable and not waived, that the Military and State Secrets privilege precluded litigation of the Contractors' "superior knowledge" claim, and that the government's claim for progress payments was not at issue in the case.

I.

A.

Now in its twelfth year of litigation, this case once again returns to this court. We have previously provided in detail the facts underlying this contract dispute. *See McDonnell Douglas Corp. v. United States,* 182 F.3d 1319 (Fed. Cir. 1999) ("*McDonnell Douglas X*"). Thus, we will only provide a summary of the relevant background here.

In 1988, the Navy awarded McDonnell Douglas Corporation ("MDC") and General Dynamics Corporation ("GD") a fixed-price contract with a ceiling price of $4,777,330,294 to research and develop a carrier-based "stealth" attack aircraft called the "A-12 Avenger." *Id.* at 1322. The full-scale engineering and development ("FSD") contract required the Contractors to design and build eight stealth aircraft according to a specified delivery schedule, with the first aircraft to be delivered in June 1990 and the remaining seven aircraft to be delivered monthly through January 1991. *Id.* The

contract also gave the Navy the option to purchase four production lots of aircraft, and the Navy exercised its option on the first production lot in May of 1990. *McDonnell Douglas XI,* 50 Fed. Cl. at 313.

From the outset, the Contractors encountered difficulties in performing the contract, especially in meeting the contract schedule and in keeping the aircraft weight within specifications. *McDonnell Douglas X,* 182 F.3d at 1322. In June of 1990, the Contractors informed the Navy that they could not deliver the first aircraft on time and that the cost of completing the contract would substantially exceed the ceiling price. *Id.* As a solution, the Contractors proposed to restructure the fixed-price agreement into a cost-reimbursement contract. *Id.* Despite their negotiations, the parties could not reach an agreement on the proposed contract restructuring or on a new delivery date. *Id.* So, in August of 1990, the Navy issued a unilateral schedule modification, continuing the first flight and delivery date to December 31, 1991. *Id.*

Subsequently, more problems arose concerning the FSD contract, leading the Department of Defense ("DoD") and the Navy to question the viability of the project. *Id.* at 1322-23. On December 17, 1990, Rear Admiral William Morris, the contracting officer, sent a cure notice to the Contractors, informing them of his intention to terminate the contract for default based on the Contractors' failure to timely fabricate the required parts and to meet specification requirements. *See id.* at 1323. In their response dated January 2, 1991, the Contractors conceded that they could not meet the new delivery schedule,

but denied that they were in default and asserted that the new delivery schedule was invalid or unenforceable. *Id.* As suggested cure, they again submitted a proposal to restructure the FSD agreement to a cost-reimbursement contract. *Id.* In exchange for that restructuring, the Contractors would absorb $1.5 billion in fixed loss and would waive their claims for equitable adjustment. *Id.*

After numerous meetings with DoD and Navy principals, Admiral Morris terminated the contract for default on January 7, 1991. *Id.* at 1323-24. A few weeks later, the Navy sent a letter to the Contractors demanding the return of approximately $1.35 billion in unliquidated progress payments under the terminated contract. *Id.* at 1324.

In June of 1991, the Contractors sought relief in the Court of Federal Claims under the Contract Disputes Act, 41 U.S.C. § 609(a) (2000). After protracted litigation, the trial court held that the Contractors' performance did not constitute the basis for the Navy's decision to terminate, and the court therefore converted the default termination into a termination for convenience. *McDonnell Douglas X*, 182 F.3d at 1324. On appeal, we reversed that judgment, holding that the termination was related to the Contractors' performance. *Id.* at 1326-29. We remanded the case to the trial court to determine whether the default termination was justified. *Id.* at 1329.

After a six-week trial on remand, the Court of Federal Claims ruled in favor of the Navy. *McDonnell Douglas XI*, 50 Fed. Cl. at 319. The trial

court sustained the default based solely on the Contractors' failure to meet the December 1991 first flight date. *Id.* at 315-19. It declined to base its determination of justified default on the Contractors' alleged financial inability to perform the contract, anticipatory repudiation, and failure to comply with weight and other specification requirements. *Id.* at 319-24. Turning to the Contractors' defenses, the trial court rejected their arguments that the unilateral schedule was unreasonable and therefore unenforceable, or, if enforceable then the Navy waived the unilateral schedule and first flight date of December 1991; that the contract was commercially impossible to perform; and that the Navy had to disclose its alleged superior knowledge despite the assertion of the state secrets privilege. *Id.* at 324-26. Having addressed those issues, the Court of Federal Claims entered judgment in favor of the government. *Id.* at 326.

After entry of judgment, the government asserted its right to immediately collect from the Contractors $1.35 billion in progress payments. Because the trial court determined that the government did not submit a counterclaim and that the unliquidated damages were not an issue in the litigation, the Court of Federal Claims ruled "it was not necessary for this court to address what we consider to be a[n] understanding among the parties that was outside the focus of this case."

The Contractors appealed the trial court's judgment and challenged the trial court's construction of our mandate, determination that the unilateral schedule was enforceable and unwaived,

and dismissal of their "superior knowledge" claims. The government cross-appealed for the return of the $1.35 billion in unliquidated progress payments. We have jurisdiction over this case pursuant to 28 U.S.C. § 1295(a)(3).

B.

We review issues of law de novo, without deference to the trial court. *Bass Enters. Prod. Co. v. United States,* 133 F.3d 893, 895 (Fed. Cir. 1998). This plenary review also applies to interpretations of our own mandate. *Engel Indus., Inc. v. Lockformer Co.,* 166 F.3d 1379, 1382 (Fed. Cir. 1999). However, we will not disturb the trial court's factual findings, such as its evaluation of evidence of default, unless they are clearly erroneous. *See Lisbon Contractors, Inc. v. United States,* 828 F.2d 759, 766 (Fed. Cir. 1987). A factual finding is clearly erroneous when the reviewing court is left with a "definite and firm conviction that a mistake has been committed." *United States v. United States Gypsum Co.,* 333 U.S. 364, 395, 68 S. Ct. 525, 92 L. Ed. 746 (1948).

II.

A.

On remand, the Court of Federal Claims sustained the default termination based solely on the Contractors' conceded inability to make the December 1991 first flight date. *McDonnell Douglas XI,* 50 Fed. Cl. at 315-19. As it explained, if it found that the first flight date was reasonable, "the Circuit's finding that the Government's decision to terminate for default was performance-related will require us to rule for defendant." *Id.* at 313. Thus,

the trial court construed our mandate as having disposed of certain issues related to the merits of the default termination and as limiting its inquiry to "whether the Navy's unilateral modification establishing a new schedule for first flight was reasonable." *Id.*

The Court of Federal Claims, however, misconstrued our mandate. Although the trial court believed that we disposed of certain issues related to the Navy's justification for the default termination, a plenary review of our opinion in *McDonnell Douglas X* belies that proposition. *See Engel Indus.*, 166 F.3d at 1382 ("We review the interpretation of our own mandate de novo.").

In *McDonnell Douglas X*, we only addressed two major issues: (1) the government's challenge to the trial court's conversion of a default termination into one for convenience; and (2) the Contractors' cross-appeal that the government was without power to terminate an incrementally-funded contract for default. *McDonnell Douglas X*, 182 F.3d at 1325-32. We did not reach the other appealed issues based on our reversal of the conversion question.

In addressing the propriety of converting the default termination, we first determined that the Court of Federal Claims misinterpreted the holding of *Schlesinger v. United States*, 182 Ct. Cl. 571, 390 F.2d 702 (1968). *McDonnell Douglas X*, 182 F.3d at 1325-26. We explained that *Schlesinger* and its progeny only barred terminations for default where there is no nexus between the default termination and the Contractors' performance under the contract.

Id. We then ruled, based on the trial court's findings of fact, that the termination of the FSD contract for default was related to the Contractors' performance of the contract and that a remand was necessary. *Id.* at 1326-29. We concluded our review of the conversion issue by stating:

> On remand, if the government can establish that Contractors were in default, then the termination for default would be valid. See *Lisbon Contractors, Inc. v. United States,* 828 F.2d 759, 765 (Fed. Cir. 1987) (holding that the government bears the burden of proof with respect to the issue of whether termination for default was justified). Conversely, if the government is not able to make this showing, then the default termination was invalid and Contractors would be entitled to a suitable recovery, presumably under a termination for convenience theory.

Id. at 1329.

After vacating the trial court's rulings on the loss-ratio and doctrine of superior knowledge in light of our disposition of the conversion question, *id.* at 1329-30, we addressed whether the government had the authority to terminate for default an incrementally-funded contract. *Id.* at 1330. On that issue, we determined that the government had that authority, holding "only that the contract, throughout its term, embodied a duty to make progress toward the ultimate end item." *Id.* at 1332. We finished that discussion by stating, once again:

> The question of whether Contractors satisfied their duty is of course that of breach, and must be determined by taking into account all of the relevant facts and testimony, such as Contractors' statements that they could not meet the contract specifications, the contract delivery schedule, nor complete performance at the specified contract price. *See supra* Part II.B. We leave it to the trial court to resolve these issues in the first instance.

Id. The conclusion section of our opinion reiterated those limited rulings and instructed the trial court to afford the parties an opportunity to litigate the legitimacy of the default termination's justification. *Id.* at 1332-33.

Our decision in *McDonnell Douglas X* did not state whether there was in fact a default. Our ruling had a limited scope, and we emphasized that point by refusing to address the merits of the government's default justification. *Id.* at 1332 ("Of course, we do not hold today that the government's default termination is justified."). Neither the text of our opinion nor its related judgment contained any indication, expressly or by intimation, that we intended to limit the default justification inquiry on remand to the reasonableness of the December 1991 delivery date. And, there is nothing in the trial court's opinion that elucidates the basis for its misinterpretation of our mandate. Therefore, we must conclude that the Court of Federal Claims misunderstood our mandate.

Because our decree does not require such a result, the trial court's finding that the unmet first flight date in December 1991 was reasonable is insufficient to sustain a default termination in this case. *See Lisbon,* 828 F.2d at 765 (stating that "the government did not, as it urges, satisfy its burden by merely showing that the contractor was behind schedule"). Consequently, the judgment in favor of the United States cannot stand on that sole ground.

Although the parties have requested that we finally dispose of this protracted litigation on appeal, the record at this point does not permit us to do so. In determining whether a default termination was justified, a court must review the evidence and circumstances surrounding the termination, and that assessment involves a consideration of factual and evidentiary issues. *See id.* at 766-67 (reviewing trial court's factual findings and decision regarding default termination for clear error). Because the Court of Federal Claims focused its ruling on the reasonableness of the December 1991 date, it did not make adequate findings on whether the Navy justifiably terminated the Contractors for default. Mindful of our limited role as a court of appeals, *Baxter Healthcare Corp. v. Spectramed, Inc.,* 49 F.3d 1575, 1585 (Fed. Cir. 1995) (emphasizing that "we sit as a court to review claims that a trial judge erred, and not as a court of first instance"), we decline to resolve this dispute on an incomplete record. Accordingly, we have no choice but to vacate the trial court's judgment and remand for further proceedings.

B.

On remand, the Court of Federal Claims must address the issue that warranted a remand in *McDonnell Douglas X*: "[W]hether the government's default termination was justified, an issue upon which we express or intimate no view." *McDonnell Douglas X*, 182 F.3d at 1321. However, the parties could not agree in this appeal on the proper legal standard applicable to that inquiry. Since the determination of legal standards is a pure issue of law, *see Bayer AG v. Schein Pharms., Inc.*, 301 F.3d 1306, 1312 (Fed. Cir. 2002) (indicating that the choice of legal standards is a legal question), we now resolve that dispute and clarify the requirements for determining whether the government has proved that the Contractors were in default.

In this case, the government's authority to terminate the contract for default derives from the incorporated terms of FAR 52.249-9. That FAR clause provides:

> (a) (1) The Government may, subject to paragraphs (c) and (d) below, by written Notice of Default to the Contractor, terminate this contract in whole or in part if the Contractor fails to-
>
> ...
>
> (ii) Prosecute the work so as to endanger performance of this contract (but see subparagraph (a)(2) below);

48 C.F.R. § 52.249-9 (1984). The plain language of the default provision permits termination whenever

the contractor fails to "[p]rosecute the work so as to endanger performance of this contract." *Id.*

The parties advance drastically opposite interpretations of this default provision. The Contractors contend that our precedent, such as *Lisbon*, permits a default termination only upon repudiation or impossibility of performance. As they explain, "a contractor's deficiencies must therefore be so severe as to be the practical equivalent of a repudiation or abandonment of the entire contract effort." Because the Contractors believe that "it must be clear that the contractor cannot or will not complete performance," they submit that it is improper to default terminate a contractor merely because it is unable to meet an interim contract milestone. The government, in contrast, argues that the interpretation of this specific default provision is an issue of first impression and that the circumstances of this case are so different that we should not seek guidance from precedent. Rather, according to the government, the default provision in this contract permits termination whenever a contractor raises concerns about its ability to satisfy a contractual requirement, such as meeting a schedule or some specification requirements. Under that construction of the default clause, the government argues that default termination was appropriate here given the Contractors' admitted inability to meet an interim contract milestone, the alleged impossibility for the aircraft design to meet contract specifications, and the Contractors' request for a restructuring of the agreement.

We disagree with the parties' interpretations of the default clause in this contract. Contrary to the Contractors' position, the default provision does not require absolute impossibility of performance or a contractor's complete repudiation or abandonment. *Discount Co. v. United States,* 213 Ct. Cl. 567, 554 F.2d 435, 441 (1977) (holding that "the default clause in this contract did not require a finding that completion within the contract's time limitations was impossible"); *Universal Fiberglass Corp. v. United States,* 210 Ct. Cl. 206, 537 F.2d 393, 398 (1976) (affirming default termination despite lack of express repudiation). Nor does the provision permit, as the government implies, default termination based solely on a contractor's concerns about meeting a contractual schedule milestone or specification requirements. *See Lisbon,* 828 F.2d at 765. Rather, the proper interpretation of the default provision lies somewhere between the parties' extreme positions, and should strike a balance between the judicial aversion to default terminations, *see J.D. Hedin Constr. Co. v. United States,* 187 Ct. Cl. 45, 408 F.2d 424, 431 (Ct. Cl. 1969) (stating that "a default termination is a drastic sanction which should be imposed (or sustained) only for good grounds and on solid evidence" (citation omitted)), and the fact that "the Government, just as any other party, is entitled to receive that for which it contracted and has the right to accept only goods that conform to the specification." *Cascade Pac. Int'l v. United States,* 773 F.2d 287, 291 (Fed. Cir. 1985) (affirming finding of default termination).

The pragmatic approach we adopted in *Lisbon* achieves that desired balance and provides the proper interpretation of the default clause. [1] Like this case, *Lisbon* involved a default termination of a contractor for failure to prosecute with diligence, despite the fact that the contractor still had time to complete performance of the contracted project. *Lisbon,* 828 F.2d at 765-66. After determining that the government bore the burden of proof in justifying a default termination, *id.* at 765, we clarified that "the government did not, as it urges, satisfy its burden by merely showing that the contractor was behind schedule." *Id.* Rather, we construed the default provision to "require reasonable belief on the part of the contracting officer that there was no reasonable likelihood that the contractor could perform the entire contract effort within the time remaining for contract performance." *Id.* (internal quotation marks and brackets omitted) (quoting *RFI Shield-Rooms,* ASBCA Nos. 17374, 17991, 77-2 BCA ¶ 12,714, 61,735 (Aug. 11, 1977), and citing *Discount,* 554 F.2d at 441). Since then, we have adopted that formulation as the controlling standard in default

[1] Although the government distances itself from *Lisbon* in this appeal, it relied on that precedent throughout the proceedings on remand. Indeed, the government urged the Court of Federal Claims to apply the Lisbon standard in its opening argument, during trial, in its closing statement, and in its post-trial briefs. Our jurisprudence does not condone such a reversal in position between trial and appeal. *See Interactive Gift Express, Inc. v. Compuserve Inc.,* 256 F.3d 1323, 1345 (Fed. Cir. 2001) ("The doctrine provides that a party will be judicially estopped from asserting a position on appeal that is directly opposed to a position that the party successfully urged at trial.").

cases involving a failure to make sufficient progress.[2] *See, e.g., Danzig v. AEC Corp.*, 224 F.3d 1333, 1336-37 (Fed. Cir. 2000) (indicating that the ASCBA properly applied the *Lisbon* standard in reviewing a default termination for failure to make progress). We again reaffirm in this case that the test

[2] This standard is accepted and applied by the contract boards and trial courts in reviewing default terminations for failure to make progress. Indeed, the Boards of Contract Appeals, whose specialized expertise with government contracts is entitled to respect, have long adopted the *Lisbon* standard in reviewing the government's default termination of contractors who allegedly failed to prosecute their work with diligence. *See, e.g., Bison Trucking & Equip. Co.*, ASBCA No. 53,390, 01-2 B.C.A. (CCH) ¶ 31,654 (2001); *Thomas & Sons, Inc.*, ASBCA No. 51,874, 01-1 B.C.A. (CCH) ¶ 31,166 (ASBCA Nov. 13, 2000); *Santee Dock Builders*, AGBCA No. 96-161-1, 99-1 B.C.A. (CCH) ¶ 30,190 (AGBCA Dec. 17, 1998); *Nat'l Interior Contractors, Inc.*, ASBCA No. 46,089, 96-2 B.C.A. (CCH) ¶ 28,370 (ASBCA May 23, 1996); *Am. Int'l Contractors, Inc./Capitol Indus. Constr. Groups, Inc.*, ASBCA No. 39,544, 95-2 B.C.A. (CCH) ¶ 27,920 (1995); *Hillebrand Constr. of Midwest, Inc.*, ASBCA No. 45,853, 95-1 B.C.A. (CCH) ¶ 27,464, (ASBCA Jan. 18, 1995); *Mich. Joint Sealing, Inc.*, ASBCA No. 41,477, 93-3 B.C.A. (CCH) ¶ 26,011 (ASBCA Apr. 26, 1993), *aff'd*,22 F.3d 1104 (Fed. Cir. 1994) (table); *Skip Kirchdorfer, Inc.*, ASBCA Nos. 32,637, 35,074, 91-1 B.C.A. (CCH) ¶ 23,380 (A.S.B.C.A. Sept.13, 1990), aff'd,944 F.2d 912 (Fed. Cir. 1991) (table); *B.M.S., Inc.*, ASBCA No. 35,430, 90-2 B.C.A. (CCH) ¶ 22,644 (ASBCA Jan. 26, 1990). Similarly, the Court of Federal Claims has applied the *Lisbon* standard in reviewing default terminations for failure to make progress. See, e.g., *Morganti Nat'l, Inc. v. United States*, 49 Fed. Cl. 110, 129-32 (Fed. Cl. 2001) (affirming default termination), *aff'd*,36 Fed. Appx. 452 (Fed. Cir. 2002); *CJP Contractors, Inc. v. United States*, 45 Fed. Cl. 343, 371 (Fed. Cl. 1999) (reversing default); *Interstate Gen. Gov't Contractors, Inc. v. United States*, 40 Fed. Cl. 585, 606-08 (Fed. Cl. 1998) (reversing default).

formulated in *Lisbon* controls the determination of whether the government justifiably default terminated a contractor for failure to make progress.

In applying that standard, we have required that the contracting officer's termination decision be based on tangible, direct evidence reflecting the impairment of timely completion. *See Lisbon,* 828 F.2d at 766 ("At trial, the government did not offer direct testimony or any other direct evidence on the time which it estimated it would take *Lisbon* to complete the contract."). In other words, a court's review of default justification does not turn on the contracting officer's subjective beliefs, but rather requires an objective inquiry. *Id.* at 766-67 (reviewing evidence underlying government's default termination). Although the contracting officer's testimony and contemporaneous documents are relevant to that determination, *id.* at 766, the trial court may also consider other factors usually relied upon by courts and contract boards, such as a comparison of the percentage of work completed and the amount of time remaining under the contract, *see, e.g., Thomas & Sons, Inc.,* ASBCA No. 51,874, 01-1 B.C.A. (CCH) ¶ 31,166 (ASBCA Nov. 13, 2000); *Nat'l Interior Contractors, Inc.,* ASBCA No. 46,089, 96-2 B.C.A. (CCH) ¶ 28,370 (1996); the contractor's failure to meet progress milestones, *see, e.g., James E. Kennedy, Tr. v. United States,* 164 Ct. Cl. 507, 512 (1964); *AAR Corp.,* ASBCA No. 16,486 *et al.*, 74-2 B.C.A. (CCH) ¶ 10,653 (A.S.B.C.A. Apr.24, 1974); problems with subcontractors and suppliers, *see, e.g., Abcon Assocs., Inc. v. United States,* 49 Fed. Cl. 678, 686-87 (2001); the contractor's financial situation,

see, e.g., Universal Fiberglass, 537 F.2d at 395-96, 398; as well as a contractor's performance history, *see, e.g., Decker & Co. v. West*, 76 F.3d 1573, 1581 (Fed. Cir. 1996); and other pertinent circumstances surrounding the decision in order to determine whether the contracting officer had a valid basis for his conclusions. *Lisbon*, 828 F.2d at 766-67; *see also Discount*, 554 F.2d at 441 ("The record is plain, however, that the default termination was not based on this demand per se but rather on the over-all evidence of Discount's failure to prosecute diligently its work under the contract."); *L & H Constr. Co.*, ASBCA No. 43,833, 97-1 B.C.A. (CCH) ¶ 28,766 (ASBCA Feb. 5, 1997) ("The Government owes the contractor no less than an assessment of all the relevant circumstances when it exercises its discretion under the default clause.").

Our precedent does not require, however, that the contracting officer be correct in his assessment, as the Contractors would have us rule. He only needs to be "justifiably insecure about the contract's timely completion." *Discount*, 554 F.2d at 441. Because the inquiry is concerned with the contracting officer's reasonable belief rather than whether he was correct, it would be impermissible "to show that after the termination action events occurred which would have permitted the contract to be completed by the delivery date." *RFI Shield-Rooms*, 77-2 B.C.A. (CCH) ¶ 12,714 (cited with approval by *Lisbon*, 828 F.2d at 765). A consideration of post-termination factors and events would transform *Lisbon's* "reasonable belief" requirement into a demand that the contracting officer have perfect foresight.

Limiting the inquiry to the time of the termination action reduces the potential for hindsight bias. *See RFI Shield-Rooms*, 77-2 B.C.A. (CCH) ¶ 12,714. Thus, the trial court should focus on the events, actions, and communications leading to the default decision in ascertaining whether the contracting officer had a reasonable belief that there was no reasonable likelihood of timely completion.

To make that determination, the Court of Federal Claims will first have to decide the actual performance that the contract requires and the amount of time remaining for performance. *See Lisbon*, 828 F.2d at 766 (faulting the government for failing to provide "direct evidence on the time which it estimated it would take [the contractor] to complete the contract."). Unless the contracting officer had determined the entire effort required under the contract and the time left to complete the contract, it would be difficult, if not impossible, for him to resolve whether "there was no reasonable likelihood that the contractor could perform the entire contract effort within the time remaining for contract performance." *Id.* at 765 (emphasis added and brackets omitted).

In this case, the parties do not agree on either of those underlying issues. They each harbor differing views of the contract completion date, ranging from the opinion that no such date existed, to the notion that the design and testing under the contract would require at least four to five years, to the suggestion that missing the first aircraft delivery date was tantamount to failing to timely complete the contract. In addition, the parties seem unsure

whether the contract solely requires delivery of the eight prototype aircraft or whether the agreement also requires delivery of the production lot purchased by the Navy under the contract's option provisions. Given those competing claims and the incomplete record before us, we leave it to the trial court to determine on first instance the actual performance required by the contract and the amount of time remaining for that performance.

To summarize, on remand, once the Court of Federal Claims determines the performance required by the contract and the contract completion date, it can then decide, in light of the information upon which the contracting officer relied in deciding to terminate for default, whether the government has met its burden of proving that the contracting officer had a reasonable belief that there was no reasonable likelihood that the contractor could perform the entire contract effort within the time remaining for performance.[3] As we explained in *McDonnell Douglas X*:

> On remand, if the government can establish that Contractors were in default, then the termination for default would be

[3] Although the parties disagreed at oral argument whether the trial court should show any deference to the contracting officer's decision, it is well-settled that the Court of Federal Claims reviews the decision to terminate a contractor for default *de novo*. *See Wilner v. United States*, 24 F.3d 1397, 1401 (Fed. Cir. 1994) (en banc) ("[I]n court litigation, a contractor is not entitled to the benefit of any presumption arising from the contracting officer's decision. De novo review precludes reliance upon the presumed correctness of the decision.").

valid. Conversely, if the government is not able to make this showing, then the default termination was invalid and Contractors would be entitled to a suitable recovery, presumably under a termination for convenience theory.

McDonnell Douglas X, 182 F.3d at 1329 (citation omitted). Whether the government has met its burden is not an issue we reach here, since it is a determination that we yield initially to the trial court and on which we neither express nor intimate any view. *See Olson Plumbing & Heating Co. v. United States,* 221 Ct. Cl. 197, 602 F.2d 950, 955 (1979) (stating that "whether the default termination is proper depends upon the facts and circumstances of each case"). Similarly, we decline to decide whether the Court of Federal Claims needs to conduct additional proceedings or admit additional evidence, as those matters are better left to the trial court's broad discretion. We merely hold and reaffirm in this case that the test we adopted in *Lisbon*, as further explained in this opinion, controls the review of default termination for failure to make progress.

III.

We now turn to the other issues raised by Contractors in this appeal. The Contractors challenge the trial court's determination that the

government's unilateral schedule was enforceable and not waived. Moreover, they contend that it was reversible error to preclude them from litigating their "superior knowledge" claim based on the government's invocation of the Military and State Secrets privilege. We address each contention seriatim.

A.

After the Contractors failed to meet the June 1990 delivery date and the parties could not agree on a new bilateral schedule, the Navy unilaterally imposed a new delivery schedule through the issuance of Modification No. P00046. Because the unilateral schedule was allegedly not reasonable, the Contractors argue that the schedule is not enforceable. We disagree.

If the government elects to permit a delinquent contractor to continue performance past a due date as it did in this case by waiving the June 1990 delivery date, *McDonnell Douglas XI,* 50 Fed. Cl. at 315, the government can establish a new contract completion date, which will serve as a basis for default termination, either through a bilateral agreement with the contractor or by unilateral action. *DeVito v. United States,* 188 Ct. Cl. 979, 413 F.2d 1147, 1154-55 (1969) If the government opts to act unilaterally, the new date that it sets must be "both reasonable and specific from the standpoint of the performance capabilities of the contractor at the time the notice is given." *Id.* at 1154. The reasonableness of the action turns on what the government "knew or should have known" at the

time it imposed the new schedule. *ITT Corp. v. United States,* 206 Ct. Cl. 37, 509 F.2d 541, 549-50 (1975).

Beyond this standard of reasonableness, our precedent does not impose the additional burdens that the Contractors would impose on the government when the United States unilaterally imposes a new completion date. Contrary to what GD contends, our precedent neither requires a determination of "what work remained to be completed as of the date the unilateral schedule was issued," nor does it necessitate an inquiry into "how long it likely would have taken the contractor to complete the remaining work, given its actual production capabilities as of the date the schedule was issued." Although those inquiries may be appropriate in certain situations, they are not requisite underpinnings for the *DeVito* reasonableness determination. Similarly, we reject the "objective achievability" paradigm suggested by the Contractors as not rooted in our precedent. Were we to adopt this new criterion, we would depart from our case law by requiring more than reasonableness; we would compel the government to have perfect prescience and be infallible in its decision. Because such an expectation is unachievable, the touchstone of this inquiry must remain grounded on reasonableness based on what the government knew or should have known when it adopted the unilateral schedule.

Based on the information available at that time, the government's unilateral schedule was reasonable. After the parties failed to agree on a

new schedule, the government proceeded to adopt a new performance schedule through a methodical inquiry. Captain Elberfeld, who prepared the schedule, conducted an independent analysis, taking into account all the issues and information then available to him. He did not solely rely on the Contractors' estimates, having lost confidence in their ability to correctly predict the schedule. Rather, he added an additional 25 percent for slippage on top of the Contractors' estimates, took into account the microcracking problems with the prototypes and the Contractors' work on resolving that issue, consulted with different qualified personnel of the Navy and the Contractors, and considered the Contractors' track-record and evidence of progress. As the trial court found, "once given his orders to develop a unilateral first flight schedule, Captain Elberfeld went about his mission in a thorough and comprehensive manner." *McDonnell XI,* 50 Fed Cl. at 318. In fact, "Captain Elberfeld set a schedule that took into account the critical information that he had at the time." *Id.* at 318-19. On that basis, the Court of Federal Claims found that the December 1991 first flight date was reasonable and enforceable. We do not see any clear error in that finding.

B.

Similarly, we agree with the Court of Federal Claims that the Navy did not waive the December 1991 first flight date. For a waiver of default to occur, there must be both a "(1) failure to terminate within a reasonable time after the default under circumstances indicating forbearance, and (2)

reliance by the contractor on the failure to terminate and continued performance by him under the contract, with the Government's knowledge and implied or express consent." *DeVito,* 413 F.2d at 1154. The application of this standard supports the conclusion of the trial court.

First, the facts do not substantiate the Contractors' allegations of forbearance based on the Navy's references to a date in the first quarter of 1992 as the first test flight date. The Navy mentioned that 1992 date on only two occasions, neither of which involves the necessary indicia of forbearance. The first time, when Captain Elberfeld mentioned the 1992 date during a presentation at the Tailhook Convention in September 1990, he was merely attempting to manage expectations and trying to provide an estimated date for planning purposes. The second time, when Captain Elberfeld told the Contractors at a Defense Acquisition Board meeting to assume a March 1992 first flight date, he made his statement contingent upon a restructured program that was being negotiated at that time but never materialized. The Court of Federal Claims, having heard the live testimony and having had the opportunity to assess the witnesses' credibility, found that those two situations did not amount to an intended forbearance. The record supports that finding, and the Contractors have not shown that trial court clearly erred.

Second, the Contractors failed to show any evidence of detrimental reliance on the government's alleged waiver. Although the Contractors spent over $100 million every month to perform the contract,

they would have done so regardless of whether their perceived deadline was December 1991 or March 1992. The significant monthly expenditure is not evidence of a change in position based on detrimental reliance; it just indicates that the Contractors were attempting to perform their contractual duties. The Contractors have not provided evidence, to this court or the trial court, that they adjusted their work or delayed their scheduled performance based on the expectation that the delivery date was four months later than December 1991. Without such evidence, we decline to disturb the Court of Federal Claims' finding that the government did not waive the December 1991 deadline.

C.

Finally, we see no error in the trial court's decision to reject the Contractors' claim of "superior knowledge." As we previously explained, "[i]n government contracts law, under certain circumstances the government owes a duty to disclose critical information to a contractor that is necessary to prevent the contractor from unknowingly pursuing a ruinous course of action." *McDonnell Douglas X,* 182 F.3d at 1329 (internal quotation marks omitted). Failure to disclose such critical information may result in a finding that the government breached its contractual duty. *Id.* However, the Court of Federal Claims determined in this case that the Contractors could not proceed with that defense, because the litigation of that claim would require extensive discovery into classified military information. *McDonnell Douglas XI,* 50 Fed. Cl. at 324-25. Specifically, the continued

litigation may involve the disclosure of classified information regarding the B-2 and F117 stealth aircraft. Because the government has satisfied the requirements for the Military and State Secrets privilege, we affirm the decision of the Court of Federal Claims on this point.

The Military and State Secrets privilege allows the United States to block discovery in a lawsuit of any information that, if disclosed, would adversely affect national security. *Crater Corp. v. Lucent Techs., Inc.*, 255 F.3d 1361, 1370 (Fed. Cir. 2001). As the Supreme Court explained,

> [t]he privilege belongs to the Government and must be asserted by it; it can neither be claimed nor waived by a private party. It is not to be lightly invoked. There must be a formal claim of privilege, lodged by the head of the department which has control over the matter, after actual personal consideration by that officer. The court itself must determine whether the circumstances are appropriate for the claim of privilege, and yet do so without forcing a disclosure of the very thing the privilege is designed to protect.

United States v. Reynolds, 345 U.S. 1, 7-8, 73 S. Ct. 528, 97 L. Ed. 727 (1953) (footnotes omitted). Courts should accord the "utmost deference" to executive assertions of privilege upon grounds of military or diplomatic secrets, and judicial review of such a claim of privilege is necessarily narrow. See *United States v. Nixon*, 418 U.S. 683, 710, 94 S. Ct. 3090, 41 L. Ed. 2d

1039 (1974). The court need only be satisfied that, under the particular circumstances of the case, "there is a reasonable danger that compulsion of the evidence will expose military matters which, in the interest of national security, should not be divulged." *Reynolds,* 345 U.S. at 10, 73 S. Ct. 528;*see also In re United States,* 872 F.2d 472, 475-76 (D.C. Cir. 1989).

Once the privilege is properly invoked by a government official with adequate authority and there is independent judicial review of the circumstances, "even the most compelling necessity cannot overcome the claim of privilege if the court is ultimately satisfied that military secrets are at stake." *Reynolds,* 345 U.S. at 11, 73 S. Ct. 528. The privilege is absolute, and "[n]o competing public or private interest can be advanced to compel disclosure of information found to be protected by a claim of privilege." *Ellsberg v. Mitchell,* 709 F.2d 51, 57 (D.C. Cir. 1983).

Thus, when the "very subject matter of the action" is a state or military secret, the action must give way to the proper invocation of the state secrets privilege. *See Totten v. United States,* 92 U.S. 105, 107, 23 L. Ed. 605 (1875) ("[P]ublic policy forbids the maintenance of any suit in a court of justice, the trial of which would inevitably lead to the disclosure of matters which the law itself regards as confidential, and respecting which it will not allow the confidence to be violated."). Although harsh, the presence of a properly invoked state secrets privilege requires dismissal of the claim that cannot prevail without the privileged information. *Reynolds,* 345 U.S. at 11 n.26, 73 S. Ct. 528; *Zuckerbraun v. Gen. Dynamics*

Corp., 935 F.2d 544, 547-48 (2d Cir. 1991) (affirming dismissal of action upon intervenor United States' proper invocation of state secrets); *Weston v. Lockheed Missiles & Space Co.*, 881 F.2d 814, 816 (9th Cir. 1989) (recognizing that state secrets privilege alone can be the basis of the dismissal of a suit); *Bentzlin v. Hughes Aircraft Co.*, 833 F. Supp. 1486, 1495-97 (C.D. Cal.1993) (dismissing case based on, inter alia, state secrets privilege); *see also DTM Research, LLC v. AT & T Corp.*, 245 F.3d 327 (4th Cir. 2001) (ruling that the quashing of subpoena on the United States that threatened state secrets did not foreclose possibility of fair trial and thus did not warrant dismissal). Because of its breadth and severe effect, the privilege should not be lightly invoked and found. *Reynolds*, 345 U.S. at 8, 73 S. Ct. 528.

In this case, the two requirements for applying the state secrets doctrine were satisfied. First, the Secretary of the Air Force made the formal assertion by submitting a declaration setting forth the reasons for invoking the privilege.[4] As he explained, discovery of the information sought by the Contractors may lead to inadvertent and unauthorized disclosure of the stealth technology unavailable in other countries and may pose a grave risk to our national security. To buttress that assertion, he also submitted to the trial court, for in camera review, a classified declaration that provided

[4] Although this case involves the Navy, the person authorized by the President in Executive Order 12,958 to determine the proper classification of information is the Secretary of the Air Force.

in more detail the specific reasons why disclosure of the information sought by the Contractors would endanger our national and military interests.

Second, after review of the declarations and the circumstances surrounding the invocation of the privilege, the trial court determined that the circumstances for the assertion were appropriate. In the original trial, a series of security breaches and discovery abuses led the trial court to conclude that litigation of the superior knowledge could not proceed. *McDonnell Douglas X*, 182 F.3d at 1329. On appeal, we vacated the state secrets determination in light of the reversal of the default termination conversion. *Id.* at 1329-30. We invoked the trial court's discretion to reconsider that issue. On remand, the Contractors' renewed discovery requests again prompted the Air Force to invoke its Military and State Secrets privilege. After considering the renewed assertion of privilege and the situation surrounding it, the Court of Federal Claims found that "[n]either the passage of time nor intervening developments have lessened the risks that prompted us to act in the first instance."

We agree with that ruling. Not only has the Secretary of the Air Force properly invoked the privilege as required by the Supreme Court, but to litigate the superior knowledge claim would require giving the Contractor's attorneys access to the classified information and ultimately divulging the information at trial. *See Fitzgerald v. Penthouse Int'l, Ltd.*, 776 F.2d 1236, 1242-44, 1242 n.8 (4th Cir. 1985) (providing that privilege requires dismissal of claim thereby preventing disclosure at trial of

classified information despite the fact that one of the parties had "personal knowledge of classified matters within the scope of the state secrets privilege"). Given the history of security breaches and discovery abuses in this litigation, *McDonnell Douglas Corp. v. United States,* 37 Fed. Cl. 270, 276-78 (Fed. Cl. 1996) (discussing pattern of security lapses during discovery, including inappropriate deposition questions by the Contractors' counsel that led to the disclosure of classified information and the use of classified information in open court and other unclassified documents), there is a risk that the military and state secret once divulged is unlikely to remain protected in this case. The public good must prevail over individual needs by enforcing the privilege and protecting the military secrets at issue here. *See Reynolds,* 345 U.S. at 11 n.26, 73 S. Ct. 528. We see no reason to fault the trial court's conclusion that the government's privilege was properly invoked and that the privilege bars further adjudication of the superior knowledge claim.

The Contractors concede that the properly invoked privilege attaches to this proceeding. Instead, they contend that the Due Process Clause of the Fifth Amendment trumps the privilege by giving them a right to present all available defenses, including the superior knowledge defense. Relying on an application of the Due Process Clause in criminal cases, the Contractors argue that the Fifth Amendment compels the government to choose between fully disclosing classified information and proceeding with the prosecution of its claim. According to the plaintiffs, because the government

refused to fully disclose the secrets, the default termination decision must be dismissed. However, in making that argument, the Contractors essentially conflate rules governing criminal and civil proceedings, elevating this civil contract dispute into the constitutional territory of a criminal prosecution. The Supreme Court has already considered the Contractors' very argument in the Military and State Secrets privilege context and rejected it:

> Respondents have cited us to those cases in the criminal field, where it has been held that the Government can invoke its evidentiary privileges only at the price of letting the defendant go free. The rationale of the criminal cases is that, since the Government which prosecutes an accused also has the duty to see that justice is done, it is unconscionable to allow it to undertake prosecution and then invoke its governmental privileges to deprive the accused of anything which might be material to his defense. Such rationale has no application in a civil forum where the Government is not the moving party, but is a defendant only on terms to which it has consented.

Reynolds, 345 U.S. at 12, 73 S. Ct. 528 (footnote omitted). The Contractors are not at jeopardy from an attack on them by the government. Rather, they are the plaintiffs in this purely civil matter, suing the sovereign on the limited terms to which it has consented. Thus, the Fifth Amendment does not re-

quire that they be able to present all defenses, including a defense that would threaten national security. Complying with the high court's edict as we must, we therefore reject the Contractors' Fifth Amendment contention.

Without a legal basis for their argument, the Contractors support their contention with practical concerns. According to the Contractors, an affirmance of the trial court's ruling on this issue would permit the government to abuse its authority as both litigant and sovereign and would lead it to use default termination as a ready alternative to terminations for convenience. For those reasons, the Contractors submit that they must have a right to either gain access to the military secrets or have the default termination vacated. We disagree. First, although the Contractors ascribe a fraudulent and deceptive intent to the government and its agents, they have not presented any evidence or corroborative facts to support their allegations. Nor have they cited any case in which the government has actually misused the Military and State Secrets privilege as they describe. Second, if we acceded to the Contractors' request and burdened the government with a duty in a civil setting to either divulge the state secrets or face an adverse disposition of the suit, we would ignore controlling precedent from the Supreme Court and authorities from other circuits that have unequivocally dismissed private claims that threatened to expose a state secret protected by the privilege. *Reynolds,* 345 U.S. at 11-12, 73 S. Ct. 528;Zuckerbraun, 935 F.2d at 547-48; *Weston,* 881 F.2d at 816; *Molerio v. Fed.*

Bureau of Investigation, 749 F.2d 815, 825 (D.C. Cir. 1984) (granting summary judgment for government after determining that the privilege was properly invoked and applied in that case); *Farnsworth Cannon, Inc. v. Grimes,* 635 F.2d 268, 281 (4th Cir. 1980) (en banc) (affirming dismissal of a contractor's suit against a Navy employee for wrongful interference with prospective contractual relations, because the court was concerned about interrogating witnesses in open court about sensitive matters); *Bentzlin,* 833 F. Supp. at 1495-97. This well-established precedent demonstrates that, when a properly invoked claim of State Secrets privilege undercuts a civil litigant's opportunity to prove its case, the interests favoring the protection of the state secret always prevail. We see no reason to deviate from this settled law.

Because the requirements for the Military and State Secrets privilege to attach were satisfied, we affirm the trial court's refusal to permit further litigation of the Contractors' superior knowledge claims.

IV.

The government also filed a cross-appeal, claiming entitlement to the recoupment of unliquidated progress payments made to the Contractors. The trial court declined to enter judgment for the government because it did not find it necessary to address that claim.

We similarly decline to rule on this premature cross-appeal. As the government admits, "[u]ntil entry of a judgment sustaining the default, our so-

called 'claim' for the unliquidated progress payments would not have been ripe." Since we vacated the trial court's judgment sustaining the default termination, the claim for a monetary judgment in the government's favor has lost its necessary predicate and is therefore not ripe for appellate review.

V.

In sum, because the Court of Federal Claims did not apply the controlling standard under *Lisbon* to this case, we vacate its ruling that the default termination was justified and remand for further proceedings consistent with this opinion. As to the Contractors' appeal of other discrete issues, we affirm the trial court's decisions on the enforceability and nonwaiver of the unilateral schedule and on the dismissal of the Contractors' "superior knowledge" claim in light of the government's proper assertion of the Military and State Secrets privilege. Finally, we decline to address or disturb the trial court's decision related to the government's claim for unliquidated progress payments.

VACATED-IN-PART, AFFIRMED-IN-PART, AND REMANDED.

APPENDIX D

United States Court of Federal Claims.

McDONNELL DOUGLAS CORPORATION
and General Dynamics Corporation,
Plaintiffs,

v.

UNITED STATES of America,
Defendant.

No. 91-1204C.

Aug. 31, 2001

OPINION

HODGES, Judge.

The issue in this case now is whether the Navy's unilateral modification establishing a new schedule for first flight was reasonable. The schedule was in place at termination, and it was specific. *McDonnell Douglas Corp. v. United States*, 182 F.3d 1319, 1332 (Fed. Cir. 1999). If it was reasonable as well, the Circuit's finding that the Government's decision to terminate for default was performance-related will require us to rule for defendant.

The unilateral schedule was reasonable. A Contracting Officer acting with discretion rationally could have determined that the contractors would not have achieved first flight by December 1991. In consideration of these factors, we dismiss plaintiffs' complaint and enter judgment for the Government.

I. BACKGROUND

The Navy introduced a program in 1984 to develop a carrier-based stealth aircraft known as the A-12. The A-12 was a full-scale engineering and development contract. McDonnell Douglas and General Dynamics contracted with the Navy in 1988 to produce eight A-12 aircraft.[1] The Navy could purchase four production lots of aircraft. It exercised this option in May 1990. Each aircraft would test different characteristics of the A-12. The eighth aircraft would possess the stealth characteristics that would serve as the basis for the optional production lots. The contract schedule called for delivery of the first aircraft in June 1990; the remaining aircraft were to be delivered monthly through January 1991.

Plaintiffs experienced difficulties in performance of this contract from the beginning. Delivery schedules and aircraft weight growth were the primary concerns. The contractors also were aware that their costs likely would exceed the ceiling price in the contract. Everyone knew in early 1990 that a June 1990 first flight could not be achieved. The Contracting Officer asked the contractors for an estimate of when the first aircraft would be delivered. Negotiations ensued, but ultimately the Navy and the contractors could not agree on a date. The Navy issued a unilateral schedule modification

[1] For a full factual background *see McDonnell Douglas Corp. v. United States*, 35 Fed. Cl. 358 (1996) (*see also McDonnell Douglas Corp.*, 182 F.3d 1319 (Fed. Cir. 1999)).

on August 17, 1990. The unilateral schedule for first flight was December 31, 1991.

The contractors asked the Navy for restructure of the contract in November 1990. The Navy issued reports during November that the Navy A-12 Program Manager was unreasonable in his conclusion that the contract could be completed within the specified ceiling price, and he failed to anticipate greater risk in the schedule. Secretary of Defense Cheney briefed the President of the United States in early December. He expressed disappointment with the Navy's handling of the A-12 program and promised to take corrective action. Thereafter, Secretary Cheney directed the Deputy Secretary of Defense to report on the status of the A-12 program within 10 days.

Secretary of the Navy Lawrence Garrett responded to Secretary Cheney's request on December 12. Secretary Garrett was concerned about the contractors' willingness to complete the contract as it was then structured. The Office of the Secretary of Defense sent a memorandum to the Navy on December 14, directing the Navy to "show cause by January 4, 1991 why the Department should not terminate the A-12 program and pursue other alternatives."

At the direction of OSD, the Navy sent a cure notice to the contractors on December 17. The Navy asserted in the notice that the contractors "failed to fabricate parts sufficient to permit final assembly in time to meet the schedule for delivery of FSED

aircraft [and] fail[ed] to meet specification requirements...."

The contractors responded to the cure notice denying they were in default of the A-12 contract. They asserted that the unilateral schedule was unenforceable and that the specifications were unachievable. The contractors also provided the Navy with a "Proposal for Equitable Restructure of the A-12 Contract." They requested the contract be restructured pursuant to Pub. L. No. 85-804.[2] In return, they would absorb a $1.5 billion fixed loss, the contract would be restructured to a cost-reimbursement contract, and they would waive their claims for equitable adjustment. The record indicates that the Under Secretary of Defense for Acquisition, Mr. Yockey, would have been willing to go forward if the contractors had agreed to accept a $2 billion loss and other concessions.[3]

Rear Admiral William R. Morris was the Contracting Officer at the time. He met with Under Secretary Yockey and Navy officials on January 4. The Chief Engineer for the Navy reported at the meeting that technical challenges on the A-12 were typical for this type of development contract, and

[2] Pub. L. No. 85-804 grants the President of the United States the power to authorize agencies or departments to provide extraordinary relief if doing so would promote national defense. *See* 50 U.S.C. § 1431 (1994). *See also McDonnell Douglas Corp.*, 182 F.3d at 1323.

[3] This suggests that Mr. Yockey at least, a major decision-maker on the scene, did not lose confidence in plaintiffs' expertise but was only haggling over price.

that the contractors could resolve remaining technical challenges. The Navy and the Joint Requirements Oversight Council re-validated the operational requirements.

Secretary Cheney met with Secretary Garrett, Under Secretary Yockey, and the Chairman of the Joint Chiefs of Staff on January 5 and decided not to grant 85-804 relief. Secretary Cheney understood that the A-12 program would be cancelled as a result, but the Navy would decide how and whether to terminate the contract. Admiral Morris met with Mr. Yockey and other Department of Defense officials on Sunday, January 6. He terminated the contract for default the next day.

Before then, Admiral Morris did not believe that 85-804 relief was the only way to proceed with the contract. He wanted the opportunity to work with the contractors. Admiral Morris had not anticipated termination of the A-12 contract.

Admiral Morris testified that under Yockey's guidelines he was not able to do what he wanted to do, which was to continue the contract. *McDonnell Douglas Corp.*, 35 Fed. Cl. at 368 n.13. The termination letter stated that plaintiffs were being terminated for "inability to complete the design, development, fabrication, assembly and test of the A-12 aircraft within the contract schedule and the Team's inability to deliver an aircraft that meets contract requirements." *Id.* at 368. The letter stated,

> the Team is in default of the contract for having failed to make progress and not meeting contract requirements. The A-12

> aircraft will not be delivered within the contract schedule nor will it meet the weight guaranty contained within the contract specification.

The contractors sued for relief on a number of bases, and the parties agreed to litigate a potentially dispositive issue first. That was Count 17, which challenged the manner in which the Navy terminated the contract for default. We ruled that the default termination was improper because we found from testimony and other evidence that Admiral Morris was not permitted to exercise reasoned discretion. *Id.* at 375. We found that the termination for default was not related to performance. *Id.* at 377. The Navy was the contracting agency, and it did not believe that the contractors' performance justified termination for default.

The Federal Circuit found that "the government's default termination was not pretextual or unrelated to Contractors' alleged inability to fulfill their obligations under the contract." *McDonnell Douglas Corp.,* 182 F.3d at 1326. The Circuit's opinion states that "the government's decision to terminate the A-12 FSD Contract for default was related to contract performance ...." *Id.* at 1326-27. It directed us to determine whether the contractors were in default of the A-12 contract. "[I]f the government can establish that Contractors were in default, then the termination for default would be valid. (citation omitted). Conversely, if the government is not able to make this showing, then the default termination was invalid ...." *Id.* at 1329.

We tried this issue for 6 weeks in May and June 2001. The Government argued that it was not limited to the bases for default found in the cure notice. That does not matter because the only reason for default that can be sustained happens to be in the cure notice: schedule. As noted above, plaintiffs would not have met the December 1991 schedule, known as P00046. We find that this schedule was reasonable.

II. DISCUSSION

A. Schedule

The default notice issued on January 7, 1991 stated that termination of plaintiffs' contract was based in part on plaintiffs' "inability to complete the design, development, fabrication, assembly and test of the A-12 aircraft within the contract schedule ...." The Federal Circuit stated that Admiral Morris believed the contractors could not meet the delivery schedule, and that he "believed [the] Contractors to be in material breach of the contract." *McDonnell Douglas Corp.,* 182 F.3d at 1327.

The schedule established by the Best and Final Offer provided that the first FSED aircraft was due in June 1990, and the remaining aircraft would be delivered monthly through January 1991. The contractors experienced problems in performance of the contract from its inception, "namely controlling the growth of the aircraft weight and meeting the contract schedule." *McDonnell Douglas Corp.,* 35 Fed. Cl. at 362. The Navy was aware in early 1990 that the contractors would not meet the delivery date for the first aircraft, but it took no action to terminate

the contract then. *Id.* "When a due date has passed and the contract has not been terminated for default within a reasonable time, the inference is created that time is no longer of the essence so long as the constructive election not to terminate continues and the contractor proceeds with performance." *DeVito v. United States,* 188 Ct. Cl. 979, 413 F.2d 1147, 1154 (1969). Defendant waived its right to terminate plaintiffs for default based on the delivery schedule set forth in the original agreement. It elected to permit plaintiffs to continue working several months past June 1990 and thereby surrendered its right to terminate for that reason. *Id.* at 1153.

The Navy issued contract modification P00046 unilaterally on August 17, 1990, setting first flight for December 31, 1991. *McDonnell Douglas Corp.*, 35 Fed. Cl. at 362. The Government seeks to uphold the default termination on the ground that the contractors were not making progress toward the December 1991 first flight schedule. Plaintiffs argue that the Navy's unilateral schedule was unreasonable and therefore unenforceable. If so, legally they could not have been terminated on that ground. Alternatively, they argue that the new schedule was waived.

The Government may terminate a contractor for default based on failure to make progress toward meeting an enforceable schedule. *FAR* 49.402-1(a). For a unilateral schedule to be enforceable, the Government must follow certain procedures when establishing the new schedule. *DeVito*, 413 F.2d at 1154. The time for performance must be "both reasonable and specific from the standpoint of the performance capabilities of the contractor at the time the notice is

given." *Id.*; *see also International Tel. & Tel., etc. v. United States,* 206 Ct. Cl. 37, 509 F.2d 541, 549 (1975). The reasonableness requirement in *DeVito* is based on what the Government "knew or should have known...." *ITT,* 509 F.2d at 550. The burden is on defendant to show that it "reestablished a new delivery schedule reasonable in the circumstances, upon a failure to comply with which it properly based the termination for default." *Jack Spires & Sons Electrical Co. Inc.*, 87-3 B.C.A. (CCH) ¶ 20,069 at 101,627, 1987 WL 45930 (Aug. 10, 1987).

The contractors argue that Captain Elberfeld, the Navy A-12 Program Manager, did not establish a reasonable schedule.[4] According to plaintiffs, the unilateral schedule was intended to serve as a "placeholder" because it did not provide revised dates for flight testing or contract completion. Moreover, plaintiffs contend that the Navy was aware that General Dynamics was having trouble manufacturing composite parts, and that the in-house system that General Dynamics was using for schedule projections was unreliable.

The contractors employed a "P/2" computer system to create an internal manufacturing schedule. Plaintiffs argue that while the P/2 system did set a first flight schedule, the system was not reliable. It did not account for manufacturing problems or unexpected technical issues, for example. Weight reduc-

[4] We have no evidence that the Contracting Officer took any part in the issuance of P00046, or even had knowledge of it. No one argued that this was an issue, however, so we do not address it here.

tion efforts and porosity problems resulted in increased complexity in the manufacture of composite structures, according to plaintiffs. They point out that the Navy did not rely on the contractors' schedule. Admiral Cook testified that by June 1990 the Navy had lost confidence in the contractors' ability to predict the schedule.

The contractors contend that even the Navy's first flight projections were slipping to the right, and that the Navy program office was projecting in August 1990 that first flight could occur in February 1992. Commander Shields' PERT system was showing a first flight in February 1992 just three days before the issuance of the unilateral schedule.[5]

"Microcracking" in certain large composite wing parts known as "big ribs" was discovered just days before the issuance of P00046 in August 1990. Plaintiffs complain that Captain Elberfeld knew about the microcracking problem but did not take that into account when he issued the unilateral schedule. The contractors also argue that the unilateral schedule was unreasonable because it required a fully specification-compliant aircraft within 16 1/2 months and required delivery of the Lot I production aircraft before the FSED test aircraft. They contend that Captain Elberfeld did not rely on the best estimates the Navy had to produce the unilateral schedule. The contractors complain that the Navy knew or should have known in August 1990 that first flight of December 31, 1991 was not achievable.

[5] PERT stands for Program Evaluation and Review Technique. Commander Shields was Captain Elberfeld's scheduling expert.

A series of events led to the issuance of P00046. Captain Elberfeld testified that in June 1990 the contractors were projecting first flight to occur between July and September 1991. The Government understood that it was not possible for the contractors to deliver the first FSED aircraft in June 1990. Mr. Lamers, the principal program manager for the McDonnell Douglas and General Dynamics A-12 Team, provided information to Captain Elberfeld in June 1990, estimating first flight in July 1991. Captain Elberfeld testified that the contractors had additional time built into the schedule-a buffer. The contractors presented briefing slides to the Government that were used to provide a schedule status. The contractors' slides stated that they had "frozen aircraft number 1, *317 configuration." Captain Elberfeld interpreted this to mean that no further design was needed for aircraft number 1. The slides also indicated that the contractors had factored in contingencies in creating span times. That is, "how long it may take to manufacture a part [and] how many tries it would take...."[6] The contractors added time to cover the unknowns. The Government considered the contractors' P/2 system to be a tool that was working effectively to estimate the schedule, according to Captain Elberfeld.

The Government made a reasoned assessment to determine whether the contractors could achieve first flight in July 1991. The Navy reviewed the con-

[6] Captain Elberfeld testified that span times are used in determining the overall flow of manufacturing in the factory. They are the "amount of time it takes to perform a particular task."

tractors' estimates and added an additional 25 percent for slippage. The Government predicted first flight to occur in November or December 1991. Shortly thereafter, Captain Elberfeld attended a meeting with Secretary Cann. Secretary Cann instructed Captain Elberfeld to get a handle on the schedule. Projected first flight kept slipping to the right and Secretary Cann wanted to know when the contractors would be ready for first flight. Secretary Cann instructed Captain Elberfeld to set a "schedule with sufficient slack."[7] Captain Elberfeld testified that he interpreted Secretary Cann's words to mean

> don't go out and try to be a big hero and have a schedule to get somewhere that is not achievable. Make sure you build in the type of contingency and buffer time that's necessary to ensure that in going forward in a restructuring we've allocated enough time that we don't need to go back and restructure and reschedule again. Give yourself the room in this first restructuring, one bite at the apple more or less.
>
> The Navy wanted a reasonable schedule, not an unachievable one. The contractors and the Navy convened a strategy board to put together a realistic schedule for first

[7] The decision to issue a unilateral schedule modification did not originate with the Contracting Officer or even with Captain Elberfeld. Neither was it the idea of his boss, Secretary Cann. Very likely the direction came from Mr. Yockey, the Acting Assistant Secretary of Defense for Acquisition.

> flight. Captain Elberfeld testified that while the Navy could not achieve a "signed-up commitment" from the contractors, he felt that they were "moving in the right direction." At the meeting, the contractors agreed to work toward an aggressive plan, but they would not sign up to a schedule. Captain Elberfeld felt that most of the technical issues affecting first flight were under control. He developed a delivery schedule for first flight that "was meant to be ... realistic [and] achievable." He stated, "with all the information we had at the time, it was an achievable schedule."

Captain Elberfeld felt that setting a unilateral schedule was the appropriate approach because

> If you don't have a delivery schedule that's realistic, you're just sort of drifting and any schedule that-any type of an interim schedule that you're planning to use along the line doesn't have any of the weight of contractual force behind it. It ends up being sort of a rubber or elastic schedule and can just move to fit the events that are taking place. Instead of trying to manage the program, you end up being run by events instead of proactively managing them.

Captain Elberfeld wanted a schedule that both the contractors and the Navy felt was one they could use to manage the program. During this period, the

contractors were proposing July-September 1991 for first flight.

John Lamers, plaintiffs' A-12 Program Manager, spoke with Captain Elberfeld on August 14 about problems with microcracking. Mr. Lamers told Captain Elberfeld that it could be a tooling or cure cycle problem and that the contractors were in the process of finding a solution. Captain Elberfeld testified that Mr. Lamers did not seem concerned and the microcracking was just one among several items he mentioned. Captain Elberfeld considered this problem but decided not to change his mind about setting the unilateral schedule for first flight for December 1991. He felt that the contractors had identified the problem and were working to fix it. He knew that contingencies and conservatism were built into the unilateral schedule, and he made a reasoned decision not to adjust the December deadline. He felt that the buffer was adequate to address the problems that the contractors were experiencing. At this time, the contractors were predicting first flight to occur *before* December 1991. Mr. Lamers testified that the contractors were "showing somewhere between September and November 1991" for first flight at the Design Review Board in September 1990.

It is likely that the December 1991 date was first mentioned by Commander Shields, Captain Elberfeld's scheduling expert. In any event, Captain Elberfeld consulted with Commander Shields before he issued P00046. Commander Shields was the Production Readiness Officer on Captain Elberfeld's team. One of Commander Shields' responsibilities was to develop schedule estimates for the Navy. He pro-

vided Captain Elberfeld information needed to update the schedule. Information was derived from different people within the Navy, as well as input from the contractors. Captain Elberfeld attended a meeting with Commander Shields and others on August 14. Commander Shields reported an inner wing problem that could lead to a February 1992 first flight if nothing were done to correct it. He also reported that a five-day work week would lead to an April first flight. The contractors were working six days a week at the time, however, and in Captain Elberfeld's words, there "may have been some coverage in the overall plan for [the inner wing issues] ... already." The Navy started with the information given to them by the contractors to predict a reasonable first flight date. The Navy looked at the contractors' past history, evidence of progress on the contract, estimates of delivery dates on tooling, estimates on composite part fabrication, and the "number of parts off a tool" to create a government estimate of first flight.[8]

It is important to note that once given his orders to develop a unilateral first flight schedule, Captain Elberfeld went about his mission in a thorough and comprehensive manner. He did not merely accept Mr. Lamers' optimistic projections on behalf of the contractors. He investigated the computer software that plaintiffs were using to estimate schedules in house. Mr. Lamers provided an explanation of his July 1991 first flight estimates by category. He noted

[8] "Number of parts off a tool" refers to the number of times it takes a contractor to manufacture a good part.

that the Contractors were including one month for "contingency" and three months for "conservatism."

The original contract terms required the contractors to begin delivery of the Lot 1 aircraft in June 1991. P00046 did not change the Lot 1 delivery schedule. This meant that delivery of the first production aircraft was required before delivery of the first test aircraft. Captain Elberfeld testified that the unilateral schedule did not establish a schedule for contract completion. Captain Elberfeld conceded that it made no sense and was not intended. The Government did not expect the Lot 1 aircraft to be delivered prior to the FSED aircraft. P00046 was intended to set the schedule for first flight, not completion of the contract.

The unilateral schedule was reasonable. Captain Elberfeld relied on input from Commander Shields as well as overall test plans made by his flight test deputy, Colonel Nyalko. Plaintiffs argued at trial that Captain Elberfeld did not consider Commander Shields' first flight estimates. However, Captain Elberfeld knew of Commander Shields' estimates. He knew that the dates were flexible; they could slip to the right or to the left. Commander Shields' dates were based on the assumption that nothing would be done about the problems. Commander Shields made hundreds of projected first flight estimates, all dependent on different assumptions. His job was to be pessimistic.[9] But Captain Elberfeld obtained information from the contractors as well. The Navy

[9] Plaintiffs did not call Commander Shields as a witness at trial.

wanted to set a schedule that the contractors could meet. Captain Elberfeld set a schedule that took into account the critical information that he had at the time.[10]

The contractors concede that they were not going to make the December 1991 first flight. Default may be sustained on this ground.

B. Schedule Waiver

Plaintiffs contend that even if the unilateral schedule was reasonable, it was waived. This is important because we have found that the schedule was reasonable and that plaintiffs would not have met it. According to plaintiffs, the Navy knew that the contractors were targeting a March 1992 first flight date. Plaintiffs point to a presentation by Captain Elberfeld and Captain Currie at the Tailhook Convention in September 1990, where they announced that first flight would occur in the first quarter of 1992. Moreover, in preparation for a meeting of the Defense Acquisition Board, Captain Elberfeld told the contractors to assume a March 1992 first flight date. According to the contractors, that is the date the Navy expected first flight; not December 1991. The contractors briefed the March 1992 first flight to the Navy and to officials in the OSD office in November 1990. The contractors told the Conventional Systems Committee in late November 1990 that a March 1992 first flight was projected. The contractors assert that they heard no objection to the March date, and

[10] Mr. Anderson, a contractor executive, acknowledged that reasonable minds could disa ee on a reasonable schedule in these circumstances.

relied on statements made during the Tailhook Convention and those of Captain Elberfeld. They continued to perform the contract with the March 1992 date in mind. Plaintiffs quote Admiral Johnson as stating that the Navy would have accepted a June or even a September first flight.[11] These communications establish that P00046 was waived, according to plaintiffs.

Captain Elberfeld testified that he briefed the Tailhook Convention on a first flight date of September 1992 "because of the security nature of the program, and ... [to] not put in something overly optimistic ... and making sure that [the aviators] wouldn't be disappointed [if first flight weren't achieved]." His statements were not intended to be a waiver of the December 1991 first flight date. He testified that a March 1992 first flight was "acceptable for a planning date, in going forward to the Defense

[11] This statement is true. The Navy would have accepted dates well beyond the March 1992 projection. Admiral Johnson was a highly credible witness and we agree that the Navy would have been satisfied with a September 1992 first flight. In fact, we have no doubt that *the Navy* was satisfied with the entire program, if somewhat frustrated with the contractors' pace. But the Circuit makes the point that *the Government* does not relinquish its right to terminate a contract merely because in this case the Navy wanted the plane. We agree. The Navy's desire to continue the contract was meant to be support for our finding that Admiral Morris was not permitted to exercise discretion in deciding whether to terminate the contract and to terminate it for *default*. Termination for default is a very serious sanction that rarely is applied by the Government. These were corporations that have a history of participation in successful and highly sensitive weapons development projects with the United States.

Acquisition Board, for the purpose of baseline-rebaselining the program." It is true that Captain Elberfeld told the contractors to assume a March 1992 first flight in preparation for a meeting of the Defense Acquisition Board. However, the parties were negotiating a restructured program at the time, and that assumption was contingent upon a restructured program. In any event, a key element of waiver is reliance. We saw no evidence that the contractors relied on a March flight deadline to their detriment. They were obligated by contract to perform regardless of the schedule.

C. Financial Ability

Defendant argued in its opening statement that the only possible way to save the A-12 program was to place additional funds into the program or into the contract. There were only two sources from which the money could have come, the Government or the contractors. The Government chose not to put additional funds into the contract, and the contractors did not have the money, according to defendant. It is defendant's position that the contractors were legally obligated to complete the contract, but "didn't have the funds to do so."

The Federal Circuit expressed its view that "[t]he cost to complete a contract-more particularly, the inability of a contractor to perform a contract at the specified contract price-and the ability to meet a contract schedule are both fundamental elements of government contracts and are related to contract performance; as such, they are highly relevant to the question of default," *McDonnell Douglas Corp.*, 182

F.3d at 1328. When terminating a contract for default the Contracting Officer is required to "give the contractor written notice specifying the failure and providing a period of 10 days ... in which to cure the failure." *FAR* 49.402-3. Case law has broadened the scope of this standard. The cure notice "need not cite each and every failure, but it must list with enough particularity the performance failures which have placed the contractor in danger of termination for default." *Composite Laminates, Inc. v. United States,* 27 Fed. Cl. 310, 318 (1992) (quoting *International Verbatim Reporters, Inc. v. United States,* 9 Cl. Ct. 710, 721 (1986)). "Where the plaintiff has received prior notice of its failures, whether by telephone, letter, or word of mouth, that information will be considered properly in conjunction with the cure notice." *Id.*

> The termination letter issued by the Navy on January 7, 1991 states that it was terminating for default because of the Team's inability to complete the design, development, fabrication, assembly and test of the A-12 aircraft within the contract schedule and the Team's inability to deliver an aircraft that meets contract requirements.... [T]he Team is in default of the contract for having failed to make progress and not meeting contract requirements. The A-12 aircraft will not be delivered within the contract schedule nor will it meet the weight guaranty contained within the contract specification.

Neither the cure notice nor the default notice suggests that the Navy thought the contractors were financially unable to complete the contract.[12] Admiral Morris did not consider plaintiffs' financial condition when deciding to terminate the contract for default. Admiral Morris testified that he "was not in a position on the basis of the information [he had] to judge the seriousness of the financial situation of either firm...." He believed that problems could be solved "within the four corners of the contract."

At trial, the Government focused its attention on McDonnell Douglas' alleged financial inability. McDonnell Douglas' financial capacity did not endanger performance on the A-12 contract, however. The Government was provided periodic reports by the Defense Contract Audit Agency (DCAA). The DCAA was charged with auditing contractors' financial status to determine whether adverse financial conditions existed that could jeopardize contract performance. The DCAA concluded in September 1990 that "MDC financial capability is weak when compared to industry standards. However, we do not believe that contract performance is endangered." The DCAA audited McDonnell Douglas again in November 1990 and made the same finding that performance was not endangered. The final DCAA audit occurred in December 1990 with the same result. Contract performance was not endangered.

[12] We held to the contrary, in fact. "The Contracting Officer did not believe that the contractors would not perform; he wanted to continue the contract and address the issues without extraordinary relief."

The Government called Mr. Neuman, a senior price analyst who was the person primarily responsible for assessing the financial condition of McDonnell Douglas during the contract period. He testified that McDonnell Douglas' cash flow situation was "almost a financial crisis...." However, Mr. Neuman conceded that he did not speak to Admiral Morris about the financial condition of McDonnell Douglas prior to termination of the A-12 contract. In fact, his office was not even consulted before the termination occurred. He was not involved in the issuance of the cure notice. He admitted that McDonnell Douglas was a viable corporate entity and at all times its available financing exceeded the amount of debt that it needed to perform its obligations. McDonnell Douglas took a number of steps to conserve cash. It participated in an inventory reduction program, curtailed capital expenditures, reduced data processing costs, cut shareholder dividends, and sold real estate. Mr. Neuman testified that none of McDonnell Douglas' government contracts were affected by its financial condition.

The Government presented evidence only with respect to McDonnell Douglas' financial position. It did not determine whether General Dynamics had the financial ability to complete the contract. Eleanor Spector, Deputy Assistant Secretary of Defense for procurement, testified that her "general feeling" was that the contract could not continue without relief under Public Law 85-804. But she conceded that in determining financial ability one must consider both contractors because the A-12 contract made them jointly and severally liable. The Government did not

perform this analysis. Ms. Spector testified that she did not have enough data before termination to determine how much cash McDonnell Douglas would have needed to continue performance. She was not aware of the borrowing capabilities of either corporation prior to termination. She did not speak to Admiral Morris about terminating the contract for default. Ms. Spector's office did not assess whether McDonnell Douglas' financial condition was contributing to a failure to make progress on the A-12 contract. Ms. Spector stated that the reasons for the default termination were Admiral Morris' and the reasons that the program would not continue "was wrapped up in a lot of other things."

Evidence at trial established that plaintiffs' financial ability was not a concern of Admiral Morris. He did not terminate this contract for financial inability of the contractors because as he testified, he was not in a position to judge their financial wherewithal. Moreover, plaintiffs' financial condition was not endangering performance of the A-12 contract. Plaintiffs' default termination may not be sustained on this ground.

D. Repudiation

The Government contends that the default termination was proper because of the contractors' "failure to provide adequate assurances that [they had] the financial capability to perform the contract constitutes repudiation of the contract." We ruled in April 1996 that the contractors did not repudiate the A-12 contract. *McDonnell Douglas Corp.*, 35 Fed. Cl. at 377. We stated that a contracting officer may termi-

nate a contract for default when the contractor has expressed a "positive, definite, unconditional, and unequivocal manifestation of intent ... not to render the promised performance when the time fixed ... by the contract shall arrive...." *Id.* (quoting *Cascade Pac. Int'l v. United States,* 773 F.2d 287, 293 (Fed. Cir. 1985)) (quoted in *United States v. Dekonty Corp.,* 922 F.2d 826, 828 (Fed.Cir.1991)). The contractors did not fail to provide adequate assurances. The Government did not view the contractors' actions in this manner. *Id.* Admiral Morris did not believe that the contractors would not perform. He wanted the opportunity to work out the problems "within the four corners of the contract."

Defendant argued in its post-trial brief that since our ruling in April 1996, "the Federal Circuit has clarified its adoption of the modern view that, in addition to traditional forms of repudiation ... a contractor's failure to provide adequate assurances that it has the financial capability to perform the contract constitutes repudiation of the contract." The Government quotes the contractors as stating that they "can't get there if we don't change the contract ... [i]t has got to get reformed to a cost type contract or we cannot do it." The contractors stated that they "could not absorb the loss that would result from the contract." Defendant argues that these statements coupled with the contractors' conduct, prove that they would not have been able to complete the contract.

Defendant cites *Danzig v. AEC Corp.,* 224 F.3d 1333 (Fed.Cir.2000) for the modern rule on repudiation. In Danzig, the Navy awarded a contract to AEC to complete construction of a Naval and Marine

Corps Reserve Training Center. AEC fell behind and the Navy issued a cure notice. At a subsequent meeting with the contractors, AEC proposed a completion date of April 16, 1991. The Navy agreed not to terminate the contract for default if AEC continued to make progress toward that schedule. AEC submitted another revised schedule of April 26, 1991. Navy accepted this schedule. The project continued to progress slowly and AEC informed the Navy that it was unable to make progress because its surety had frozen its bank account. The Navy issued a cure notice stating that AEC needed to complete the work by the agreed schedule. AEC responded by explaining that the work would not be complete by the April deadline. Due to financial constraints with its surety AEC could not predict when the project would be completed. Unless the surety released funds, AEC stated that "it is doubtful that AEC will ever be able to complete the project." The Navy responded by asking AEC to provide another detailed response. AEC again stated that it "cannot cure the deficiency ... we cannot give you any assurance as to when the project will be completed." The Navy issued a show cause letter to AEC asking why the contract should not be terminated for default. AEC never responded to this request, and on April 22, 1991 the contract was terminated for default.

The Federal Circuit reasoned that the termination for default was proper because AEC "failed to give the Navy adequate assurances that it could complete the contract on a timely basis or even that it could continue to make progress toward completion." *Danzig*, 224 F.3d at 1337. The Federal Circuit

noted that AEC "removed the contract files and office equipment from the work site and disconnected the telephone at the work-site office." *Id.* at 1339. AEC's conduct, coupled with its responses did not provide the Navy with assurance that the project would be completed. While AEC asserted that the Government was at fault for some delay, it did not explain why this caused slow progress. *Id.* For all these reasons, the Federal Circuit concluded that AEC had breached the contract.

None of those facts is present here. In response to the cure notice issued by the Navy, the contractors stated that they were committed to the program and were providing a response to the concerns raised by Admiral Morris. The contractors addressed Admiral Morris' cure letter and provided additional information about the progress of the program. Certain specifications and delivery schedules would not be met, but the contractors explained why this was so. They alleged that certain requirements were impossible to satisfy, for example. Unlike AEC, McDonnell Douglas and General Dynamics continued to perform until they were terminated for default. They were spending between $120 and $150 million per month on the A-12 contract.

Ms. Spector testified that the contractors never refused to perform. The contractors spent money other than that provided by the Government through progress payments. Admiral Morris testified that McDonnell Douglas wanted to solve the problems within the contract. He believed that it was possible to work with the contractors to find a solution. "The contracting officer did not believe that the contrac-

tors would not perform; he wanted to continue the contract and address the issues with the contractors without extraordinary relief." *McDonnell Douglas Corp.*, 35 Fed. Cl. at 377. Admiral Morris did not view the contractors' response to the cure notice as failing to provide adequate assurances.

The Government points to the contractors' request for equitable restructure of the A-12 contract as evidence that their financial situation would not permit the contractors to complete this contract. The proposal for restructure was not a response to the cure notice. It was a request for financial assistance. It was not included with the cure notice response but was a separate document with a separate cover sheet. Admiral Morris took notes at a January 2, 1991 meeting with the contractors. He records Mr. Anders, Chairman-Elect of General Dynamics, as stating, "[b]oth companies committed." Yockey agreed that contractors were "mov[ing] in the right direction."

Failure to give adequate assurances does not appear in the termination notice as a ground for default. While the contractors wanted a restructured program they did not state they would suspend work on the A-12 contract. John McDonnell, CEO of McDonnell Douglas, testified that the contractors "weren't about to abandon [the A-12 contract]." Admiral Morris testified that he "would not have terminated the contract on the 7th of January if I got the authority to give it one more try."

Plaintiffs did not repudiate this contract. Admiral Morris did not terminate the A-12 contract because

the contractors did not give adequate assurances. Default may not be sustained on this ground.

E. Weight

The termination notice includes the assertion that the contractors' inability to meet the weight guaranty was a reason for default. The original weight specification was waived by the Navy. We ruled that 7930 pounds over BAFO was acceptable to the Government. *McDonnell Douglas,* 35 Fed. Cl. at 362 If the parties argued this holding on appeal, the Circuit did not address it.

Waiver requires that (1) the Government has knowledge of performance that does not conform with contract requirements; (2) the Government through action or inaction indicates that the nonconforming performance is acceptable; and (3) the contractor relies on the acceptance and continues to perform the contract. *Gresham & Co., Inc. v. United States,* 200 Ct. Cl. 97, 470 F.2d 542, 553-55 (1972); *DeVito,* 413 F.2d at 1153-54.

Defendant accepted the overweight condition of the aircraft. *McDonnell Douglas,* 35 Fed. Cl. at 373.[13]The Navy knew in September 1989 that the contractors would not meet the BAFO weight requirement. *Id.* The Navy encouraged the contractors in October 1989 to "stop worrying about weight and to focus on manufacture and assembly" of the aircraft. *Id.* In May 1990, the Navy determined that the A-12 aircraft weight would be 7930 pounds over

[13] *See McDonnell Douglas,* 35 Fed. Cl. at 373, for a complete set of factual findings.

BAFO. *Id.* The Navy knew that the original predicted weight was unachievable. *Id.* The Contractors notified the Navy in a June 1990 letter that the BAFO estimate would not be met, and asked that the contract be revised. *Id.* We held that the letter "documents the contractors' belief that the BAFO weight had been waived." *Id.* The Navy was only concerned that it receive an aircraft that met its operational needs. *Id.*

The Navy knew that the weight of the aircraft was 7930 pounds over BAFO. The contractors continued to perform. The weight specification in the contract was waived.

F. Other Specifications

The Government asserted at trial that the contractors were in default of specifications not identified in the cure notice or the default notice. This includes PA Roll, the Propulsion System, and Structural Certification. The propulsion system includes three components: the air inlet, the engine, and the exhaust nozzle. PA Roll is power approach roll, which refers to the aircraft's ability to roll its wings as it approaches a carrier for landing. The Government also refers to "substantial and continuous" delay by the contractors, which they assert was present throughout the life of the A-12 contract. The Government contends that these alleged problems endangered successful completion of the A-12 contract.

The default notice states vaguely that the contractors' "inability to deliver an aircraft that meets contract requirements" is a basis for default. Admiral Morris did not terminate this contract for the con-

tractors' inability to meet the PA Roll, the Propulsion System, or Structural Certification. He did not even consult with technical personnel before termination. *McDonnell Douglas Corp.*, 35 Fed. Cl. at 368.

More importantly, plaintiffs were not in default of these specifications. The contractors' Chief Engineer, Dr. Keith Jackson testified that PA Roll met the original contract specification. Dr. Jackson briefed Admiral Gentz on the risk reduction efforts that the contractors had taken with respect to PA Roll. These efforts had the potential to improve the A-12's roll performance beyond that required in the contract specifications. General Dynamics' project pilot for the A-12 program, Mr. Sweeney, believed that PA Roll performance was within the specification. He believed that the A-12 PA Roll performance would be carrier suitable.

The Contractors were making progress with respect to the A-12 propulsion system. Mr. Squires, the Government's A-12 Project Engineer on the propulsion system, testified that he was unaware of termination concerns with respect to propulsion issues. He testified that "[termination] caught [him] totally by surprise." The Navy was aware that in sub-freezing conditions ice could break off from the aircraft inlet and strike the engine. The contractors were not required to perfect anti-icing until aircraft 11. The FSED aircraft that was scheduled to fly in December 1991 did not require the anti-icing procedures. Admiral Cook agreed that the contractors had successfully completed the Critical Design Review in 1989 on the engine. Technical risks associated with the engine were regarded as low at termination. The contractors

were solving problems with the engine mixer. Admiral Cook reported to Under Secretary Yockey that resolution of the mixer problem was a "low-tech fix." The contractors were making progress on the development and testing of the exhaust nozzle. The contractors were performing tests on the nozzle and additional testing was planned. The contractors' problem with nozzle development was not a "showstopper."

The Government contends that structural certification of the A-12 aircraft was another requirement that the Contractors were not meeting at termination. [14]However, Admiral Lockard sent a memorandum to Admiral Gentz in November 1990 reporting that "the A-12 structural certification plan has been agreed to by [the Navy] and the contractors...." Admiral Cook's briefing to Secretary Yockey just before termination rated the overall structure status as "low/medium risk." The contractors had a plan in place and they were making progress with regard to structural certification.

The Government cites 63 other specifications that the contractors were failing to meet at the time of termination. The contractors identified the 63 specifications in July 1990, and the Navy elected to go forward with the contract. The Navy did not terminate the contract then. At Critical Design Review III (CDR III) on October 18, 1990, Admiral Lockard announced that the parties had "reached a technical

[14] Structural certification is the process of confirming that an aircraft is capable of withstanding loads and stresses during aircraft operation.

resolution on the airplane." Admiral Lockard believed that the path to successful close out of CDR III was in place and "if both parties agreed to follow the path ... we would ... wind up concluding CDR with successful results."[15] Soon after termination of the A-12 contract for default, Admiral Cook responded to a draft report of the Inspector General of the Department of Defense as follows:

> [W]hile there were a number of technical concerns identified during the third phase of the CDR ... none were viewed as insurmountable. In fact, in the ensuing months (July to November) all issues were resolved to the satisfaction of the Navy's technical community.

We ruled that "the Navy believed that the aircraft would meet operational requirements." *McDonnell Douglas Corp.,* 35 Fed. Cl. at 371. The contractors were not terminated for failure to meet these 63 requirements. The technical issues were resolved to the satisfaction of the Navy. Default may not be sustained on this ground.

III. CONTRACTORS' DEFENSES

A. Superior Knowledge

We ruled in December 1996 that certain issues related to plaintiffs' superior knowledge defense could not be tried because the resulting threat to national

[15] The Government contends that because the minutes of CDR III were not signed it was never closed out. Irrespective of closeout, the contractors were expected to build the aircraft as defined during the CDR process. They did that.

security would not permit it. This determination was based in part on the Government's invocation of the state secrets doctrine and partly on "a series of security breaches and discovery abuses...." *McDonnell Douglas Corp.*, 182 F.3d at 1329. The Federal Circuit asked us to reconsider that Order, but the circumstances that prompted the ruling persist. Therefore, we must reaffirm the December 13, 1996 Opinion and Order for the reasons states therein.

The Federal Circuit's opinion speculated that some of the restrictions on superior knowledge issues would be removed by now, "[b]ecause of the passage of time and of possible intervening developments ...." *Id.* at 1330. The Circuit questioned "whether the risk of disclosure of state secrets will preclude adjudication, on remand, of Contractors' superior knowledge claim, and the issues of loss adjustment and reasonable profit." *Id.* But after that, the parties conducted discovery and exchanged contention interrogatories in preparation for trial. In the course of that discovery, plaintiffs issued several interrogatories that prompted the United States to invoke again the military and state secrets doctrines to protect information that is necessary to resolution of these issues.

We reviewed the declaration by Secretary of the Air Force F. Whitten Peters, and determined that it comports with the legal requirements for invoking the state secrets doctrine as set forth by the Federal Circuit. We also reviewed the classified version of Secretary Peters' declaration, and we remain satisfied that superior knowledge issues in this case cannot be litigated safely. This determination is based on that declaration and the warnings described, as

well as those of previous government officials.[16] We know from recent briefings that all of these warnings continue to apply with full force.

We cannot establish that the information that has been removed from this case would have benefitted either party. Without extensive discovery related to this information, which will not be permitted for years if ever, no one can know whether either party would have been helped or harmed by it. At one time plaintiffs made a persuasive showing that they could prove their claim without the information. Years later, defendant made the same argument, that it did not need the protected information to defend the superior knowledge count of plaintiffs' complaint. Neither side was entirely right or entirely wrong. We can never know enough to make a finding of fact on this issue. That is why we could not try claims or defenses that depend on information that has been removed from this case.

[16] *See also* McPeak Declaration at 2-3 (July 22, 1993) ("I have concluded that continued inquiry into what is known as plaintiffs' 'superior knowledge' claims would necessarily require examination and use of information that cannot be disclosed in this litigation."); *see also* Donley Declaration at 5-6 (March 30, 1993) ("[i]nadvertent, unauthorized disclosure of the information that is described in more detail in my in camera declaration could severely jeopardize national security."); *see also* Rice Declaration at 4-5 (November 20, 1992) ("The unauthorized disclosure of the national security information at issue reasonably could be expected to cause extremely grave damage to the national security .... this will weaken our country's ability to defend itself and could place at risk our aircraft and the lives of the crews of those aircraft.")

Other reasons for removing the superior knowledge issues from this case are set out in *McDonnell Douglas v. United States,* 37 Fed. Cl. 270 (1996). All of those reasons apply today. The Appendix to which we referred in earlier orders and opinions remains classified under seal at the Pentagon. The reviewing court may wish to retrieve that document should it have the occasion to reach this issue again. However, the parties do not have access to this document and it is not included in the record otherwise.

Issues involving superior knowledge cannot be litigated safely. Defendant's argument that it is entitled to a loss adjustment pursuant to *FAR* 49.203 and plaintiffs' lost profits argument are moot. Plaintiffs may not use superior knowledge as a defense because we cannot know whether that argument has merit.

B. Impossibility

Plaintiffs now argue that the Government's invocation of the state secrets doctrine has prevented litigation of their impossibility defense. Information withheld by the Government "bore directly on the achievability of the weight, other technical performance, and schedule provisions of the A-12 Contract ..." according to plaintiffs, and they cannot prove impossibility because superior knowledge is an element of that defense. However, neither this new argument nor the cases cited by plaintiffs fit the facts of this case.

Plaintiffs argue that the court's ruling that the BAFO weight was "unachievable" provides additional evidence that the contract was impossible to perform.

Yet we did not rule that the BAFO weight was unachievable. *The Navy* thought the BAFO weight was not achievable. So did everyone else. In any event, the BAFO weight is not an issue because we have ruled that it was waived as a contract specification. Similarly, other specifications are not in issue because failure to meet specifications was not a reason that would have supported the contracting officer's decision to terminate for default.

Plaintiffs' best argument is "commercial impossibility" as explained by the Court of Claims in *Foster Wheeler Corp. v. United States,* 206 Ct. Cl. 533, 513 F.2d 588 (1975). A contract is commercially impossible if it "could not be accomplished without commercially unacceptable costs and time input far beyond that contemplated in the contract." Defendant's argument that plaintiffs were approaching the ceiling price of their contract would offer support to such a theory. That is not the argument before this court, however, and no evidence was submitted to support it.

The potential issue of an impossibility defense arose in a pre-trial hearing. Defendant was concerned that evidence of impossibility could be presented after defendant rested its case. We ruled that if plaintiffs were to raise a defense of impossibility, defendant could put on a rebuttal case to address that evidence.[17] Plaintiffs did not present such evi-

[17] Plaintiffs' counsel stated that the Government should put on the default case, and "if we put [the impossibility defense] in ... he can come back and defend. If ... we don't come forward with impossibility, he's got nothing to defend against."

dence. In fact, plaintiffs' position has been that building the A-12 was not impossible; it would have flown in March 1992.[18]

IV. CONCLUSION

The United States asked two major defense contractors with impeccable credentials and long histories of government service to undertake a complex and highly sensitive research and development project involving stealth technology. It worked closely with those contractors on a daily basis, on all aspects of the design and manufacture. It worked through the Navy because the Navy was the contracting agency. For reasons that do not appear in the record of this case in their entirety, the Government abruptly terminated the contractors for default.

Admiral Morris, the Navy contracting officer did not want to terminate the contract between the Navy and contractors. He wanted to work out all the problems within the four corners of the contract, as he put it. He was not allowed that option. We found that Admiral Morris had no choice but to terminate the contract. He also felt that he had to terminate for default-a grievous sanction. The Federal Circuit ruled that Admiral Morris terminated the contract for performance-related reasons, and that his actions were products of his independent discretion. That being the law of the case, we must rule for defendant. This is so because the unilateral schedule was reasonable, and if the Contracting Officer was concerned about

[18] We stated at trial that "plaintiffs' position seems to be that not only was it possible, but you were well on your way to building this ship."

whether the contractors would meet the schedule, that concern is a legitimate basis for terminating the contract for default.

The Clerk will enter judgment for defendant. No costs.

APPENDIX E

United States Court of Appeals,
Federal Circuit.

McDONNELL DOUGLAS CORPORATION,
Plaintiff-Cross Appellant,

and

General Dynamics Corporation,
Plaintiff-Cross Appellant,

v.

UNITED STATES,
Defendant-Appellant.

Nos. 98-5096, 98-5122, 98-5123.

July 1, 1999.
Rehearing and Suggestion for Rehearing En Banc
Denied Oct. 29, 1999.

CLEVENGER, Circuit Judge.

This dispute arises out of the government's default termination of a contract between the United States Navy and defense contractors McDonnell Douglas Corporation and General Dynamics Corporation ("Contractors") to develop a carrier-based, low-observable "stealth" aircraft known as the A-12 Avenger. After several years of litigation, the United States Court of Federal Claims held that the gov-

ernment's termination of the contract for default could not be sustained because the government did not exercise the requisite discretion before entering a default termination, *see McDonnell Douglas Corp. v. United States*, 35 Fed. Cl. 358, 368-71 (1996) (hereinafter *McDonnell Douglas IV*), and converted the termination for default into a termination for convenience, awarding Contractors costs totaling $3,877,767,376. *See McDonnell Douglas Corp. v. United States*, 40 Fed. Cl. 529, 555-56 (1998) (hereinafter *McDonnell Douglas IX*). We hold that, because the termination for default was predicated on contract-related issues, it was within the discretion of the government. Accordingly, the Court of Federal Claims' conversion of the termination for default into a termination for convenience was in error. We reverse the trial court's judgment and remand the case to the trial court for a determination of whether the government's default termination was justified, an issue upon which we express or intimate no view.

I

A

In 1984, the Department of the Navy introduced the Advanced Tactical Aircraft Program, known as the A-12 program, to develop a carrier-based stealth aircraft for the Navy. In January 1988, Contractors entered into a Full Scale Engineering Development contract (the "A-12 FSD Contract") with the government to produce eight FSD aircraft at a target price of $4,379,219,436. *See McDonnell Douglas IV*, 35 Fed. Cl. at 361. The contract was structured as an incrementally funded, fixed-price incentive contract

with a ceiling price of $4,777,330,294, and recited a schedule of installment payments over the five-year term of the contract. The first aircraft was originally scheduled to be delivered in June 1990, and subsequent aircraft were to be delivered each month through January 1991. *See id.* at 361-62.

From the outset, Contractors encountered difficulties in performing the contract. Particular problems included meeting the contract schedule and keeping the aircraft weight within specifications. At the beginning of 1990, the Department of Defense initiated a Major Aircraft Review to evaluate various major aircraft programs in view of recent changes around the world and the corresponding reduced threat to national security. *See id.* at 362. The A-12 program was included in this Review, and Defense Secretary Richard Cheney visited the McDonnell Douglas plant as part of the review process. By the early part of 1990, the Navy's contracting officer knew that Contractors would not meet the delivery date for the first aircraft. *See id.* However, although Secretary Cheney was apprised of some concerns in the A-12 program, the review concluded that there was a continuing need for the A-12 and that the Navy should pursue the program. *See id.* at 363. Secretary Cheney reported these results during his testimony before Congress in April 1990.

In June 1990, Contractors informed the Navy that they could not meet the contract schedule, that the cost of completing the contract would substantially exceed the ceiling price, and that Contractors could not absorb the loss that would result from the contract. Contractors asserted that a fundamental

problem with the FSD contract was its structure as a fixed-price contract and proposed that the contract be modified. Thereafter, Contractors submitted a proposal to change the contract schedule, but the Navy and Contractors failed to reach an agreement on that issue. Instead, on August 17, 1990, the Navy unilaterally issued a contract modification that changed the delivery schedule for the aircraft. Under this modification, the delivery date of the first aircraft was delayed until December 1991, and the remaining aircraft became due periodically between February 1992 and February 1993. *See* Contract Modification P00046 ¶ 1(b), Joint Appendix at 15,657.

In November 1990, Contractors submitted a formal request to the Navy to restructure the contract as a cost-reimbursement type contract. At the end of the same month, two reports were published which documented the handling of the A-12 program under the Major Aircraft Review. The Navy's "Beach Report," dated November 28, 1990, found that the A-12 program manager had been unreasonable both in reaching a conclusion that the contract could be performed within the ceiling price and in evaluating the risk of failing to meet the contract schedule. *See McDonnell Douglas IV,* 35 Fed. Cl. at 363. The Beach Report criticized several Navy officials involved in the A-12 program. Separately, a November 29, 1990 Department of Defense Inspector General report concluded that problems in the A-12 program were inaccurately identified during the Review because the Review did not accord with specified procedures and was otherwise handled poorly. *See id.*

During the Secretary's briefing to the President of the United States in early December 1990, the Secretary indicated his disappointment with the Navy's handling of the A-12 program and promised to take appropriate actions. On December 3, the Secretary directed the Deputy Secretary of Defense to review and report on the status of the A-12 program within ten days. This resulted in several meetings by the Defense Acquisition Board and Defense Procurement Review Boards. In addition, on December 12, the Secretary of the Navy responded to Secretary Cheney's December 3 request with a memorandum that expressed concern about Contractors' ability and willingness to perform under the contract, and which noted in particular Contractors' belief that the government should assume responsibility for failure to meet goals under the contract, and that the government should restructure the contract. The memorandum concluded with a statement that the Navy would examine whether the contract should be terminated for default, and would make a recommendation to the Secretary by January 5, 1991. *See id.*

On Friday, December 14, Secretary Cheney directed the Secretary of Navy to show cause by January 4, 1991 why the A-12 program should not be terminated. The following Monday, December 17, the Navy issued a cure notice to Contractors stating that unless they were able to meet contract specifications by January 2, 1991, the government might choose to terminate the contract for default. In particular, the cure letter stated that, *inter alia,* Contractors had "failed to fabricate parts sufficient to permit final assembly in time to meet the schedule for delivery,"

and had "fail[ed] to meet specification requirements." Joint Appendix at 16,524. The letter asserted that "[t]hese conditions are endangering performance of [the] contract." *Id.*

High-level meetings between the responsible government personnel, including the contracting officer and the general counsels of the Department of Defense and of the Navy, and Contractors, including the Chief Executive Officers of McDonnell Douglas and General Dynamics, occurred on December 18 and 21. During these meetings, Contractors asserted that they "[c]an't get there if we don't change contract," *id.* at 16,533, and "[i]t has got to get reformed to a cost type contract or we cannot do it." *Id.* at 16,549. When asked by the government on December 21 "can you correct deficiencies to provide an aircraft that meets the requirements," Contractors replied "[a]ll deficiencies cannot be corrected. Can we deliver a satisfactory aircraft for the Navy? Mother nature won't allow correction of all defects. We'll do the best we can and the Navy has to decide if that's good enough." *Id.* at 16,548-49.

Contractors responded to the cure notice on January 2 by admitting that they "[would] not meet delivery schedules or certain specifications of the original contract, or the revised FSD delivery schedule." *Id.* at 18,175. Contractors did not contest that they had failed to fabricate parts in time to meet the delivery schedule for the FSD aircraft. Nonetheless, Contractors asserted that they were not in default because, in their view, the delivery schedules were invalid or unenforceable. *See id.* at 18,175-78. As suggested cure, Contractors submitted a proposal to

restructure the contract, pursuant to which Contractors would absorb a $1.5 billion fixed loss on the cost overrun from the contract, the contract would be restructured to a cost reimbursement contract, and Contractors would waive their claims for equitable adjustment. Contractors proposed to restructure the contract pursuant to Pub. L. No. 85-804, which gives the President of the United States the power to authorize departments or agencies connected with national defense to grant extraordinary relief under contracts if such an action facilitates the national defense. *See* 50 U.S.C. § 1431 (1994).

On Saturday, January 5, Secretary Cheney met with Undersecretary of Defense for Acquisition Yockey, the Secretary of the Navy, and the Chairman of the Joint Chiefs of Staff to discuss the budget and the A-12 program. At the meeting, Secretary Cheney noted that a scheduled payment of $553 million-one of the largest installment payments under the A-12 contract-was due on Monday, January 7. Later that day, Secretary Cheney, acting under authority pursuant to Pub. L. No. 85-804, decided not to grant relief. On Sunday, January 6, Undersecretary Yockey informed Rear Admiral William R. Morris, who at this time was acting as contracting officer over the A-12 contract, that Secretary Cheney had denied 85-804 relief and that no further funds would be obligated under the A-12 program. The next day, Admiral Morris issued the termination letter to Contractors stating that the government was terminating the A-12 contract due to Contractors' default.

B

On February 5, 1991, the Navy sent a letter to Contractors demanding the return of approximately $1.35 billion in unliquidated progress payments under the terminated contract. On June 7, Contractors filed suit in the United States Court of Federal Claims under the Contract Disputes Act, 41 U.S.C. § 609(a) (1994), requesting that the court: (1) grant their equitable adjustment claims dated December 31, 1990, (2) convert the government's termination for default into a termination for convenience, (3) deny the government's demand for return of progress payments, (4) award Contractors costs and a reasonable profit under the contract, (5) award them settlement expenses, and (6) award damages for breach of contract. *See McDonnell Douglas Corp. v. United States,* 25 Cl. Ct. 342, 346 (1992).

After several years of litigation in the Court of Federal Claims, that court ruled, in a decision dated April 8, 1996, that the government's default termination was invalid according to *Schlesinger v. United States,* 182 Ct. Cl. 571, 390 F.2d 702 (Cl. Ct. 1968). *See McDonnell Douglas IV,* 35 Fed. Cl. at 368-71. The trial court held that under *Schlesinger,* the government is required to exercise "reasoned discretion" before terminating a contract for default, and that the government failed to meet this requirement because the Secretary of Defense's actions effectively forced the Navy to terminate the A-12 contract for default. *See id.* at 369-71. Therefore, the trial court vacated the government's termination for default and converted it into a termination for convenience. *See id.* at 361.

In further litigation over damages, Contractors claimed that they were entitled to recover a reasonable profit under the contract, whereas the government argued that any recovery should be reduced by an appropriate loss-adjustment ratio. Contractors further alleged that the government possessed knowledge regarding how difficult it would be to perform the A-12 contract, and that under the "superior knowledge" doctrine, the government had a duty to either disclose such knowledge or otherwise protect Contractors against suffering unreasonable losses under the contract. The court held that the government's claim for a loss adjustment, Contractors' claim for reasonable profits, and the superior knowledge claim could not be further litigated because of the government's invocation of the "state secrets doctrine," *see McDonnell Douglas Corp. v. United States,* 37 Fed. Cl. 270, 272 (1996) (hereinafter *McDonnell Douglas V*), which grants the Executive the exclusive right to bar discovery into specific classified areas that affect state secrets. *See United States v. Reynolds,* 345 U.S. 1, 7, 73 S. Ct. 528, 97 L. Ed. 727 (1953). The court ultimately denied the government's claim for return of $1.35 billion in unliquidated progress payments, and allowed Contractors total costs under the contract of approximately $3.88 billion. Taking into account progress payments of some $2.68 billion that had already been paid to Contractors, the court entered judgment of approximately $1.2 billion in favor of Contractors. *See McDonnell Douglas IX,* 40 Fed. Cl. at 555-56.

The government appeals from the trial court's decision to convert the default termination to a termi-

nation for convenience, and from the trial court's refusal to apply a loss-adjustment ratio in calculating damages. Contractors conditionally cross-appeal the trial court's ruling, arguing that the government has no power to terminate an incrementally-funded contract for failure to make progress toward a goal that has not yet been funded. Contractors also assert that their recovery cannot be reduced by a loss-adjustment factor based on the estimated cost of completing work that was never funded. We have jurisdiction pursuant to 28 U.S.C. § 1295(a)(3).

II

The level of discretion that must be exercised by the government before terminating a contract for default is a question of law, which we review *de novo*. *See Darwin Constr. Co. v. United States,* 811 F.2d 593, 596 (Fed. Cir. 1987); *Barseback Kraft AB v. United States,* 121 F.3d 1475, 1479 (Fed. Cir. 1997). We will upset the trial court's factual findings, however, only if they are clearly erroneous. *See, e.g., Bass Enters. Prod. Co. v. United States,* 133 F.3d 893, 895 (Fed. Cir. 1998).

A

The trial court held that the government's termination of the A-12 contract did not comport with the rule laid down in *Schlesinger* by the United States Court of Claims, our predecessor court, for a proper default termination. *Schlesinger* involved a cap manufacturer who won a contract to supply the Navy with 50,000 service caps for enlisted men. The contract required the manufacturer to submit preproduction samples of component materials, as well

as two samples of the completed cap, to the government for approval prior to production. In addition, the contract included a delivery schedule which set forth delivery dates for five separate installments of the completed caps. *See Schlesinger,* 390 F.2d at 703-04. Schlesinger did not submit the two sample caps and certain thread for pre-production approval, perhaps because he had fulfilled a contract for 240,000 identical Navy caps the previous year. Schlesinger also failed to deliver the first installment of caps as specified in the delivery schedule. *See id.* At the time, Schlesinger was also a prime suspect in an ongoing United States Senate subcommittee investigation regarding textile procurement irregularities within the military. Indeed, Schlesinger testified before the subcommittee during the pendency of his supply contract; shortly after his testimony, the chairman of the subcommittee sent a letter to the Navy implying that Schlesinger's contract should be terminated. This information was communicated to the contracting officer, who promptly terminated Schlesinger's contract. *See id.* at 705-06.

The Court of Claims held that the default termination of Schlesinger's contract was illegal. In doing so, the court first found that Schlesinger was indeed technically in default under the terms of the contract. *See id.* at 706-07. However, the court determined that neither the contracting officer nor anyone else in the Navy exercised independent judgment in terminating the contract for default. *See id.* at 707-08 (citing *John A. Johnson Contracting Corp. v. United States,* 132 Ct. Cl. 645, 132 F. Supp. 698, 704-05 (1955)). Thus, the court found that the con-

tractor's "bare" or "technical" default "served only as a useful pretext for the taking of action felt to be necessary on other grounds unrelated to the [contractor's] performance...." *Id.* at 709.

The illegality in *Schlesinger* stemmed from the Navy's reliance on contractor default as a pretext to terminate its relationship with the contractor, independent of the state of actual performance under the contract. The court characterized Schlesinger's performance shortcomings as merely a "technical default" or "bare default," *id.* at 707, 708, and emphasized the Navy's total failure to consider the level of performance once it found a means for terminating by default. *See, e.g., id.* at 708 ("[T]he Navy acted as if it had no option but to terminate for default ... once the mere fact of non-delivery was found."). In *Schlesinger,* it was improper for the Navy to terminate the contractor for default due solely to pressure from a congressional oversight committee because this ground for termination was totally unrelated to contract performance.

In short, *Schlesinger* bars only a termination for default in which there is no considered *nexus* between the default termination and the contractor's performance under the contract. A second case relied upon by Contractors, *John A. Johnson Contracting Corp. v. United States,* 132 Ct. Cl. 645, 132 F. Supp. 698 (1955), also supports this rule. In *Johnson,* the plaintiff contractor failed to complete construction for Army hospital buildings in a timely fashion because of bad weather that had rendered certain construction roads unusable. The construction roads had previously been contracted out to a different contrac-

tor. *See id.* at 699-700. After numerous delays, the contracting officer determined that both the roads and buildings should be completed by a single contractor, and therefore decided to terminate the plaintiff's contract. Although the contracting officer intended to terminate the plaintiff's contract for convenience, he ultimately terminated the contract for default because government lawyers informed him that a nondefault termination would create legal problems. *See id.* at 705. Because the *Johnson* court found that the contracting officer had already decided to terminate the plaintiff for convenience, it held that the change to a termination for default "did not represent [the contracting officer's] judgment as to the merits of the case." *Id.* Indeed, because the court found, as a factual matter, that the plaintiff could not be held at fault for the unforeseen conditions, *see id.* at 703-04, there could be no proper nexus between a termination for default and the plaintiff's performance.

A third case cited to us by Contractors, *Darwin Construction Co. v. United States,* 811 F.2d 593 (Fed.Cir.1987), further confirms the rule identified above. In *Darwin,* we adopted the Armed Services Board of Contract Appeals's finding that "the default action was taken solely to rid the Navy of having to deal with Darwin." *Id.* at 596 (internal quotation marks omitted). Thus, we held that the government used Darwin's technical default as a mere pretext for terminating the contract on grounds unrelated to performance. *See id.* Furthermore, *Darwin* clarifies what is meant by the "reasonable discretion" test used in *Schlesinger* and *Johnson.* In *Darwin,* we

stated that, although a contracting officer has discretion with respect to contract termination, a termination for default will be set aside if it is arbitrary or capricious, or constitutes an abuse of the contracting officer's discretion. *See id.* at 598. When there is no nexus between the decision to terminate for default and contract performance, as was true in *Darwin, Schlesinger,* and *Johnson,* the termination for default may be arbitrary and capricious and set aside in favor of a termination for convenience.

Properly understood, then, *Schlesinger* and its progeny merely stand for the proposition that a termination for default that is unrelated to contract performance is arbitrary and capricious, and thus an abuse of the contracting officer's discretion. This proposition itself is but part of the well established law governing abuse of discretion by a contracting official. *See, e.g., United States Fidelity & Guaranty Co. v. United States,* 230 Ct. Cl. 355, 676 F.2d 622, 630 (1982) (listing four factors to be used in determining if conduct by a government official is arbitrary and capricious: (1) evidence of subjective bad faith on the part of the government official, (2) whether there is a reasonable, contract-related basis for the official's decision, (3) the amount of discretion given to the official, and (4) whether the official violated an applicable statute or regulation).

B

The record shows that the government's default termination was not pretextual or unrelated to Contractors' alleged inability to fulfill their obligations under the contract. Therefore, unlike the cases cited

above, the government's decision to terminate the A-12 FSD Contract for default was related to contract performance, and the Court of Federal Claims erred by converting the termination into one for convenience without first addressing the question of breach.

First, the trial court interpreted the Navy's actions prior to termination to evince a desire *not* to terminate the A-12 program for default, but rather to continue the contract. *See McDonnell Douglas IV*, 35 Fed. Cl. at 370. For example, the trial court noted that the government had overlooked Contractors' alleged default for several months, had unilaterally modified the contract to excuse the missed delivery date for the first aircraft, and had determined that even though the aircraft would be overweight, it would still meet operational requirements. *See id.* at 370, 373-74. Moreover, the trial court noted that the Navy "did not contemplate issuing a cure notice in December [1990]" and "did not believe the contractors' performance justified termination." *Id.* at 370.

The trial court's factual findings do in fact establish that the Navy did not want to terminate the A-12 program. Instead, at all times up until the very end, the Navy hoped to preserve the program and its A-12 aircraft. That is not to say, however, that Contractors were not in default under the contract, or that the government did not have the right to terminate the contract for default. A party to a contract, faced with a breach by the opposing party, can choose either to terminate the contract or to continue the contract, perhaps extracting other concessions or consideration from the breaching party in return for its willingness to modify the contract. *See, e.g.*, 3

Samuel Williston & Richard A. Lord, A Treatise on the Law of Contracts § 7:36 (4th ed.1992). A party that chooses to proceed with the contract-even if it is the government, and even if it manifests a strong desire to procure the item that is the subject of the contract-does not thereby waive its right to terminate for default. Indeed, the trial court's finding that the Navy went to great lengths to preserve the A-12 program suggests that it would not have terminated the contract but for its belief that Contractors had breached the contract or would not perform the contract.

More importantly, however, the record demonstrates that the government properly terminated the A-12 program for reasons related to contract performance. Admiral Morris, the contracting officer, testified at length about his decisional process that led to the termination for alleged default. He thought that he had three choices: to terminate for convenience, to terminate for default, or to do nothing. He rejected the latter as "irresponsible," thus focusing his attention on the other two choices. He eliminated the termination for convenience first, because he believed Contractors to be in material breach of the contract. This was so, in his words, because, as conceded in Contractors' response to the cure notice:

> They were in default because they acknowledged they would not be able to achieve the contract specifications and the contract requirements. Two, they had indicated that the would not be able to meet the delivery schedule that was currently in the contract. And three, they

> would not be able to perform the contract without extraordinary relief or additional funding for the contract. So they basically said they can't perform under the contract and they were in default of it.

Joint Appendix at 3,898-99. In further elaboration of his decision, again in the context of Contractors' response to the cure notice, Admiral Morris testified as to why he thought Contractors' default was material:

> They had failed to fabricate parts so as to endanger performance of the contract, and in my judgment, as would relate to the production options, failed to make progress, and it was clear to me that that is where they stood on the 7th of January when I terminated the contract for default.

Id. at 3,917. As to why a termination for convenience was inappropriate, Admiral Morris stated that:

> [B]ecause I felt very strongly that as a result of the contractors' default, it would be nothing short of unconscionable for me to put the burden of the contractors' failure to make progress and the contractors' failure to fabricate parts, so as to endanger performance of the contract, put that burden on the government and the taxpayer to reimburse all costs and to pay the contractors a profit for their failures.

Id. at 3,920. Therefore, Admiral Morris terminated the contract for failure to make progress and for failure to meet contract requirements.

Failure to meet contract specifications and inability to meet the contract delivery schedule are of course relevant considerations to whether a contractor is in default. *See Discount Co. v. United States*, 213 Ct. Cl. 567, 554 F.2d 435, 441 (1977) (inability to meet specifications); *Universal Fiberglass Corp. v. United States*, 210 Ct. Cl. 206, 537 F.2d 393, 398 (1976) (failure to meet schedule); *see generally* John Cibinic, Jr. & Ralph C. Nash, Jr., Administration of Government Contracts 929-35 (3d ed.1995) (discussing the requirements for a default termination based on failure to make progress); *id.* at 953-60 (discussing anticipatory repudiation by a contractor, such as "nonperformance and claims for payments or relief from matters as to which the contractor had assumed the risk").

The trial court also found that Secretary Cheney denied extraordinary relief, which led to the termination, because of concerns about the A-12 program's "cost and schedule." *McDonnell Douglas IV*, 35 Fed. Cl. at 372. The cost to complete a contract-more particularly, the inability of a contractor to perform a contract at the specified contract price-and the ability to meet a contract schedule are both fundamental elements of government contracts and are related to contract performance; as such, they are highly relevant to the question of default.

The government had specific concerns about when-and if-the A-12 aircraft would ever be delivered and how much it would cost. Secretary Cheney stated in testimony before Congress that the A-12 program was terminated because "no one could tell me how much the program was going to cost even

just through the full-scale development phase or when it would be available. Data that had been presented at one point a few months ago turned out to be invalid and inaccurate." *Hearings on National Defense Authorization Act for Fiscal Years 1992 and 1993-H.R. 2100 and Oversight of Previously Authorized Programs Before the House Comm. on Armed Servs.*, 102nd Cong. 60 (1991) (statement of Richard Cheney, Secretary of Defense). The evidence in the record demonstrates that the Secretary of Defense denied relief under Pub. L. 85-804, and Admiral Morris chose to terminate the contract for default, for reasons related to Contractors' state of performance of the contract. The trial court emphasized that although Contractors failed to meet the aircraft weight limit, the Navy essentially waived this requirement because the overweight aircraft would still meet all operational requirements. *See McDonnell Douglas IV*, 35 Fed. Cl. at 363, 376. However, although that finding is relevant to the ultimate determination of whether Contractors were in breach, or whether a breach was excused, it is insufficient to show, in light of all the other evidence in the record, that the government terminated the contract for reasons wholly unrelated to contract performance.

We think it clear beyond any doubt that Admiral Morris, unlike the contracting officer in *Schlesinger*, or in other cases that have upset terminations for default for lack of nexus to contract performance behavior, made his choice for reasons related to contract performance. Admiral Morris certainly knew that Contractors took another view of events tran-

spiring during contract performance: although they admitted that they could not perform the contract according to its terms, they felt that the fault for their failure should be laid at the government's feet. Admiral Morris meant not to take away the right of Contractors to assert their defenses to termination for default, he instead only meant to assert the government's right to allege material breach on the record of contract performance that had been laid before him by Contractors themselves. Given the reasons stated for the action taken by the contracting officer in this case, it was legal error for the trial court to see these facts as commanding conversion of the termination for default into one for the convenience of the government.

To summarize, the government may not use default as a pretext for terminating a contract for reasons unrelated to performance; instead, there must be a nexus between the government's decision to terminate for default and the contractor's performance. The record and the facts found by the trial court establish that the government denied additional funding for the A-12 program and terminated the contract for default because of concerns about contract specifications, contract schedule, and price-factors that are fundamental elements of contract performance. Therefore, the trial court erred by vacating the termination for default without first determining whether a default existed. On remand, if the government can establish that Contractors were in default, then the termination for default would be valid. *See Lisbon Contractors, Inc. v. United States*, 828 F.2d 759, 765 (Fed. Cir. 1987) (holding that the

government bears the burden of proof with respect to the issue of whether termination for default was justified). Conversely, if the government is not able to make this showing, then the default termination was invalid and Contractors would be entitled to a suitable recovery, presumably under a termination for convenience theory.

III

We turn next to the government's argument that the trial court erred in refusing to apply a loss ratio to Contractor's termination for convenience recovery, and the trial court's related treatment of Contractors' claims under the superior knowledge theory and for reasonable profits. In government contracts law, under certain circumstances the government owes a duty to disclose critical information to a contractor that is necessary to prevent the contractor from unknowingly pursuing "a ruinous course of action." *Helene Curtis Indus., Inc. v. United States,* 160 Ct. Cl. 437, 312 F.2d 774, 778 (1963). This doctrine of superior knowledge is well established in law, *see, e.g., Hardeman-Monier-Hutcherson v. United States,* 198 Ct. Cl. 472, 458 F.2d 1364, 1371-72 (1972); *Helene Curtis Indus.,* 312 F.2d at 778 & n.1, and failure to disclose crucial information can lead to a finding of contract breach by the government, *see, e.g., GAF Corp. v. United States,* 932 F.2d 947, 949 (Fed. Cir. 1991). In this case, the government resisted Contractors' superior knowledge claims on the ground that the government could not have an implied duty to reveal classified information pertinent to the A-12 program that would threaten national security. The trial court denied the government's mo-

tion to dismiss the superior knowledge claims on the pleadings and allowed Contractors limited discovery. *See McDonnell Douglas V*, 37 Fed. Cl. at 275-76.

After a series of security breaches and discovery abuses, the trial court concluded that it could not litigate further the related issues of loss adjustment, superior knowledge, and reasonable profits. *See id.* at 272, 276-78. Contractors do not directly appeal this ruling; they contend only that if we upset the trial court's decision on loss adjustment, a remand of all three is appropriate. The government argues that Contractors' superior knowledge and reasonable profits claims were properly removed from litigation because they jeopardized state secrets, but that its loss adjustment claim could be litigated without this danger and should have been allowed to proceed. Because we conclude that the trial court erred in converting the government's default termination of the A-12 FSD Contract to a termination for convenience, whether a loss adjustment applies to termination for convenience damages is not ripe for our decision. Because of the passage of time and of possible intervening developments, we are in no position to judge whether the risk of disclosure of state secrets will preclude adjudication, on remand, of Contractors' superior knowledge claim, and the issues of loss adjustment and reasonable profit. We think the trial court must be free to adjudicate the government's defense of its termination for default in the manner most fair and just to the parties. The trial court thus is free to reconsider this issue on remand. We express no view on the trial court's previous ruling on

whether these three interrelated issues may be litigated.

IV

Turning finally to Contractors' cross-appeal, we consider whether the nature of the A-12 contract as a fixed-price, incrementally-funded contract affects the government's ability to terminate the contract. Contractors first argue that the government cannot apply a loss adjustment factor, based on the estimated cost of completing the contract, to Contractor's recovery under a termination for convenience because the government was not obligated to fund the contract to completion. Because we reverse the trial court's conversion of the default termination to a termination for convenience, we do not address this point.

Contractors similarly argue that the government cannot legally terminate the A-12 FSD Contract for failure to make progress toward work that the government was not obligated to fund, and which it in fact did not fund in full. Contractors argue that because the government limited its potential liability to Contractors through the incremental funding arrangement, *see* A-12 FSD Contract, ¶ H-7(c), Joint Appendix at 15,073, there was no mutuality of obligation for the full FSD contract, and the contract was only valid to the extent of the funds already obligated. Under Contractors' theory, it follows that the government could not terminate the contract for failure to make progress toward work that they were not legally obligated to perform. In essence, Contractors assert that the government was precluded from terminating them for default due to failure to make

progress toward the completion of the A-12 contract, unless and until the government had funded the contract in full.

We reject Contractors' arguments, however, for the following reasons. First, the A-12 FSD Contract explicitly recites the grounds upon which the government may terminate the contract for default, which grounds include Contractors' failure to make progress. *See* 48 C.F.R. § 52.249-9(a)(1)(ii) (1984); A-12 FSD Contract § I ¶ I, Joint Appendix at 15,251 (incorporating FAR 52.249-9). Contractors agreed to installment funding of the contract because the government could not obligate the full ceiling price at the time of contracting. *See id.* § H-7(a), Joint Appendix at 15,072. In order to comply with the Anti-Deficiency Act, *see* 31 U.S.C. § 1341(a) (prohibiting expenditures, obligations, and contracts exceeding appropriations), the parties specified that the government's total obligation, including termination costs, would never exceed the amount obligated at the time of termination. *See* A-12 FSD Contract § H-7(c), Joint Appendix at 15,073. In return, Contractors were not required at any time to incur costs in excess of the total obligated amount. *See id.* § H-7(b), Joint Appendix at 15,072. Despite this funding arrangement, however, the parties agreed that the government had the right to "terminate this contract in whole or in part if the Contractor fails to ... [p]rosecute the work so as to endanger performance of this contract." 48 C.F.R. § 52.249-9(a)(1)(ii) (1984). Therefore, installment funding did not contractually manifest itself as a condition to Contractors' performance; it merely stated a term characterizing the

performance of the government. Moreover, the terms of the contract make clear that failure to make progress was a valid basis for default termination.

Second, we disagree with Contractors regarding their obligations under the A-12 FSD Contract. Contractors emphasize that, because of the incremental funding, there has never been a binding contract for completion of full FSD performance. Contractors acknowledge that the government could have default terminated the contract for failure to meet specific requirements associated with a particular installment of funding, but assert that failure to meet such specific requirements constitutes the *only* basis for a valid default termination. Because the contract did not link any specific objectives to a particular level of funding, Contractors argue, there was no basis for a default termination. We agree with Contractors that, at the time of termination, they were not obligated to *complete* all contract requirements. That does not mean, however, that Contractors did not have any obligations with respect to the full FSD requirements. As we noted above, the A-12 FSD Contract recites failure to make progress as a basis for contractor default and contract termination. *See*48 C.F.R. § 52.249-9(a)(1)(ii) (1984). Therefore, Contractors' assertion that failure to meet contract requirements that are linked to already-funded work is the sole basis for default is simply incorrect. Failure to satisfy such requirements forms a ground for default under 48 C.F.R. § 52.249-9(a)(1)(i) (stating that the government may terminate a contract for default if the contractor fails to "[p]erform the work under the contract within the time specified in this contract or

any extension"). Subsection (a)(1)(ii), in contrast, provides a separate basis for default: it obligates Contractors to make enough progress so that contract performance is not endangered. *See Universal Fiberglass Corp.*, 537 F.2d at 398 (Ct. Cl. 1976) ("Failure to make progress is obviously something different from failure to deliver, or else the default clause would not provide separately for both."). The A-12 FSD Contract makes clear that this is a continuing obligation that exists even though the contract has not yet been funded to completion.

Third, the authorities cited by Contractors fail to establish that they were under no contractual duty to make progress. Contractors rely heavily on an internal government memorandum prepared by the Defense Department's Contract Finance Committee to support their proposition that a fixed-price incrementally funded contract imposes no obligations on a contractor beyond those associated with funding that has already been provided. The memorandum expresses the committee's view that:

[I]f incremental funding is used, the contractor cannot be required to expend any effort beyond the Government's limitation of obligation. Failure to provide additional funding increments not only results in contract termination, but also makes it necessary to define, after the fact, what part of the effort should have been completed for the amount of funding actually provided. Since this division was apparently not possible in the first place, the contract, for all practical purposes, is converted to a best effort cost-type vehicle; the Government gets whatever the contractor was able to complete with the money pro-

vided.... Any advantages gained from use of a fixed price R & D contract are at risk until that point when incremental funding is replaced with full funding.

Memorandum from Chairman, Department of Defense Contract Finance Committee, to Director, DAR Council ¶ 3(c) (June 5, 1992), Joint Appendix at 68,695 (emphasis added). Setting aside questions about the legal significance of this memorandum, we conclude that Contractors' duty to make progress toward completing the A-12 FSD contract is consistent with the views expressed in the memorandum. Unlike the obligation to complete performance, which arises only when the contract has been fully funded, Contractors' duty to make progress is a continuing obligation associated with each payment installment, and thus is not an "effort beyond the Government's limitation of obligation." *Id.*

Having determined that Contractors were obligated to make enough progress such that contract performance was not endangered, we must now address what progress Contractors should have made, corresponding to the funding actually provided by the government, in order to avoid default for failure to make progress. We disagree with Contractors' argument that it is "not possible" to answer this question, and that the contract must be converted into a cost-reimbursement type contract. *Id.* In litigation over a contractor's failure to make progress-unlike a dispute over failure to meet a specific contract requirement or schedule-courts must always determine *ex post* the threshold of performance that a contractor must meet to avoid endangering performance of a

contract. *See* Cibinic & Nash, Administration of Government Contracts 930-32 (tracing the evolution of the test applied by courts for failure to make progress). The same is true in this case.

Contractors rely on *Electronics of Austin,* ASBCA No. 24,912, 86-3 BCA ¶ 19,307 (1986), for the proposition that they were under no duty to make progress. In that case, the Board of Contract Appeals found that the government had waived the original contract performance schedule and therefore "there was no time frame within which [the plaintiff] had to perform." *Id.* at 97,631. Because there was "no time frame" at all for performance, the Board held that the plaintiff could not be guilty of failing to make progress. *Id.* In the instant case, however, there was a specified delivery schedule, including the delivery of the first FSD aircraft in December 1991. *See* A-12 FSD Contract § F, Joint Appendix at 15,049 (initial delivery schedule for the eight FSD aircraft); Contract Modification P00046 ¶ 1(b), Joint Appendix at 15,657 (Aug. 17, 1990) (revised delivery schedule). Therefore, the contract imposed a duty on Contractors to make such progress so as not to endanger performance as long as the contract was in place, that is, as long as the contract was being funded. *See* 48 C.F.R. § 52.249-9(a)(1)(ii) (1984). Consequently, Contractors' protestations to the contrary, we do not "view the contract that existed prior to full funding as embodying the 'ultimate end item' of the full FSED effort." Reply brief of Plaintiffs-Cross Appellants at 6. Instead, we hold only that the contract, throughout its term, embodied a duty to make progress toward the ultimate end item.

The question of whether Contractors satisfied their duty is of course that of breach, and must be determined by taking into account all of the relevant facts and testimony, such as Contractors' statements that they could not meet the contract specifications, the contract delivery schedule, nor complete performance at the specified contract price. *See supra* Part II.B. We leave it to the trial court to resolve these issues in the first instance.

CONCLUSION

We reverse the trial court's ruling that the government's default termination of the A-12 FSD Contract must be converted into a termination for convenience because the government did not exercise the necessary discretion. Of course, we do not hold today that the government's default termination is justified. As Contractors correctly point out, they have never been found to be in default of the contract. Because the trial court focused on the legitimacy of the government's default termination decision, rather than on whether Contractors were in fact in default, the parties have not yet been afforded the opportunity to fully litigate default. *See McDonnell Douglas Corp. and General Dynamics Corp. v. United States,* No. 91-1204C, slip op. at 2 (Fed. Cl. June 17, 1993). If the government fails to establish at trial that Contractors were in default under the contract, then the government's default termination would be improper and Contractors could rightfully recover damages under the theory of a termination for convenience. We vacate the trial court's ruling that the government's loss adjustment claim and Contractors' superior knowledge claim and claim for

profits may not be litigated. Finally, we reject Contractors' argument that the incremental funding found in the A-12 FSD Contract precludes the government from terminating the contract for failure to make progress.

REVERSED-IN-PART, VACATED-IN-PART, AND REMANDED.

APPENDIX F

United States Court of Federal Claims

McDONNELL DOUGLAS CORPORATION
and General Dynamics Corporation,
Plaintiffs,
v.

UNITED STATES of America,
Defendant.

No. 91-1204C.

OPINION AND ORDER

March 30, 1998.

HODGES, Judge.

INTRODUCTION

Plaintiffs McDonnell Douglas and General Dynamics entered into a full-scale engineering and development (FSED) contract with the Navy in 1988 to develop the A-12, a Stealth aircraft. The Navy terminated the contract for default in 1991. We ruled that the termination for default was improper and converted it into a termination for the convenience of the Government. *See McDonnell Douglas Corp. v. United States*, 35 Fed. Cl. 358 (1996). The purpose of this opinion is to set forth our reasons for awarding plaintiffs most of the costs that they incurred in performing the A-12 contract.

BACKGROUND

"[I]f, after termination, it is determined that the Contractor was not in default, or that the default was excusable, the rights and obligations of the parties shall be the same as if the termination had been issued for the convenience of the Government." *Federal Acquisition Regulation (FAR)* 52.249-9(g). We approach this situation as if the Government had terminated this contract for convenience on January 7, 1991-the date of the default termination.[1]

Plaintiffs argued that the *FAR* entitles them to incurred costs plus a reasonable profit, while defendant urged us to adjust plaintiffs' cost reimbursement amount downward to reflect the loss that they would have sustained had the contract been completed. When the Government terminates a contract for its convenience, the contractor "should be compensated fairly for the work done and the preparations made for the terminated portions of the con-

[1] *FAR* 52.249-9(g) is a fiction that has not operated smoothly in this case. A contracting officer who has just terminated a contractor for default is not interested in considering the same contractor's claim for termination for convenience settlement costs. Nor is the contracting officer likely to participate in subcontractor settlements as provided by *FAR* 49.108-7 ("Government assistance in settling subcontracts"), if he assumes that the contractors will be responsible for all of the subcontractor settlements. That is what happened here. The contracting officer declined to participate in the contractors' settlement discussions with subcontractors, thereby giving plaintiffs an "estoppel" argument on that issue. We did not address estoppel, but ruled that the settlements presumptively were appropriate if the Government could not show collusion or less than arms-length bargaining.

tract, including a reasonable amount for profit." *FAR* 49.201. Typically, the contractor is entitled to recover all of its incurred costs and settlement costs, and reasonable profits if warranted. *See FAR* 52.249-2(f). If it appears that the contractor would have suffered a loss on the entire contract, however, the contractor would not obtain a profit, and its cost recovery is reduced according to the rate of loss. *See id; see also McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 270, 272-73 (1996). For reasons stated in a December 1996 ruling, however, we did not allow profit or consider to what extent a loss ratio might apply. *See McDonnell Douglas Corp.*, 37 Fed. Cl. at 272. We could not consider plaintiffs' Requests for Equitable Adjustment for similar reasons. *See Id.* at 272. During trial in June and July 1997, we considered only the costs plaintiffs incurred by performing the A-12 FSED contract, Lots I, and II options, and "wind-up" termination costs.

Plaintiffs presented a termination for convenience claim for $3.992 billion, excluding profit and interest and before application of the "funding cap."[2] The

[2] We determined that the incremental funding clause (H-7) of the contract limits plaintiffs' cost recovery to the funds obligated at the time of termination: $3,499,793,515. *See McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 295, 297 (1997), modified,39 Fed. Cl. 665 (1997). When adjusted for funding obligated for Incentive Price Revisions and Economic Price Adjustments (IPR/EPA), the total funding cap is $3,635,767,376. *See McDonnell Douglas Corp. v. United States*, 39 Fed. Cl. 665, 672-73 (1997) (finding that additional funding was obligated to cover approximately $135 million pursuant to an Economic Price Adjustment Clause and an Incentive Price Revision Clause.) Lots I and II were separate provisions in the A-12 contract that were not governed by the incremental funding clause.

$3.992 billion in costs include: $3.750 billion for the FSED portion of the contract, $.212 billion for Lot I, and $.030 billion for Lot II.[3] Plaintiffs submitted their certified termination for convenience claim on a total cost basis in June 1991. Later updates covered costs incurred in the interim, such as subcontractor settlements.

The funding cap imposed by the court limits recovery to $3,499,793,515 for the FSED portion of the contract. Additional funds obligated through the Incentive Price Revision and Economic Price Adjustment clauses raise the funding cap to $3,635,767,376. Adding to this amount the $.212 billion for Lot I and $.030 billion for Lot II, which are undisputed amounts "outside" of the cap, we arrive at $3,877,767,376, the highest award possible with the funding cap in place. Unless the Government's valid challenges would bring the amount claimed by plaintiffs below this figure, findings detailed below have little practical effect.

Recovery under Lots I and II is not in dispute. *See McDonnell Douglas Corp.*, 37 Fed. Cl. at 297 n.2.

[3] Under the contract, plaintiffs were to produce eight FSED aircraft. The contract also provided the Navy an option to purchase four production lots of aircraft. Each FSED aircraft would test different characteristics of the A-12; stealth capabilities would be verified in the "fully capable, fully equipped" eighth aircraft that would serve as the basis for the production lots. Under the original agreement, the first FSED aircraft would be delivered in June 1990; the rest would be delivered monthly through January 1991. The Navy exercised its option on the first production lot on May 31, 1990. *See McDonnell Douglas Corp.*, 35 Fed. Cl. 358, 362 (1996).

The parties asked us to determine plaintiffs' total incurred costs, irrespective of the cap. If the funding cap is higher or does not apply, plaintiffs' reasonable, allowable, and allocable costs total $3,978,002,676. Otherwise, plaintiffs may recover no more than $3,877,767,376.

Problems with the Coopers & Lybrand (Miller) Report

The Government hired Coopers & Lybrand to audit plaintiffs' incurred costs. This effort was managed by Frederic R. Miller, an auditor who was the Government's only witness at trial.

The Government's challenges to plaintiffs' claimed costs are based entirely upon the Miller Report. Plaintiffs supplied proof with respect to all of their claimed costs to some degree, but more in some areas than in others. Some of these costs could not be awarded if strict accounting standards were employed. We believe that the FAR does not limit such costs to a rigid application of cost accounting standards.

Plaintiffs attacked Mr. Miller's experience and credibility along with the usefulness of his report. General Dynamics contended that Miller had no personal knowledge and experience with the program. He was "denied access to the very government personnel who were familiar with it," such as the program manager, contracting officer and class desk. Additionally,

Miller had no experience working for an aircraft design company and no prior experience with an RDT & E program that had been terminated. Miller

had only a general sense of what the A-12 contract required; he did not have the necessary security clearances to know what it specifically required. Miller lacked familiarity with the requirements, schedule, and terminology of the A-12 research and development contract, including such issues as concept formulation, DEM/VAL, IDR, PDR, CDR, concurrency, how many radars were required, how many test aircraft were required, how many change orders occurred, when first flight was, and when and how the contract schedule changed. Despite this inexperience, [Coopers & Lybrand] consulted with no one in the Navy who had been involved with the A-12 program for technical assistance-not Captain Elberfeld, not Captain Cook, not Mr. Mutty, and not Admiral Morris. Miller conceded that such information could be competent evidence for an auditor to consider, but observed that he did not have access to such people.... Indeed, the government instructed C & L not to consult with such Navy personnel.

Plaintiffs' problems with Miller's report do not stop there. General Dynamics questions, inter alia, Miller's level of experience/familiarity with the "25% rule" that applies to items being returned to vendors for restocking, Inventory Verification Reports, and plant clearance officers. According to General Dynamics, Miller "did not consider relevant FAR and DCAA Contract Audit Manual ... provisions before questioning plaintiffs' post-termination relocation expenses."

Miller's report claims to represent the "independent and objective opinions of [Coopers & Lybrand] regarding plaintiffs' termination for convenience

claim." Plaintiffs question this assessment.[4] General Dynamics observes that "[d]uring the drafting of the May 1995 reports, Miller consulted with, and received comments from the Department of Justice in order, in Miller's words, 'to make sure we were all singing from the same sheet of music in terms of the final report.' "

Mr. Miller's analysis was helpful but marginally useful in determining the proper level of incurred costs. He acknowledged that the audit involved making determinations that were "straight up and down accounting type of decisions.... We viewed our role as providing ... only an audit report that was advisory ... in nature, and that we wouldn't be making ultimate determinations that either the TCO or the person sitting in the place of the TCO would have to make." Defendant's counsel confirmed, "Miller has not been offered to provide opinions under [FAR] 49.201.... Mr. Miller is here to testify and we're offering him to testify regarding his conclusions as to allowability, allocability and reasonableness under FAR part 31." Miller understood that his role was to provide accounting advice and his opinion regarding FAR Part 31, but that the court's inquiry must include a consideration of FAR Part 49 as well.

Tension Between FAR Part 31 and FAR Part 49

Defendant argued that FAR Part 31 should be the focal point of the court's analysis; plaintiffs emphasized *FAR* Part 49. FAR 49.113 provides that "[t]he

[4] A note contained in the auditors' workpapers states the following: "Limit the positive comments (actually none), we want 'negatives.' What is wrong with the proposal."

cost principles and procedures in the applicable subpart of Part 31 shall, subject to the general principles in 49.201, ... be used." (emphasis added). *See also Codex Corp. v. United States*, 226 Ct. Cl. 693, 698-99, 1981 WL 27970 (1981). Part 31 generally may be described as establishing a formulaic, accounting-based structure, while Part 49 provides an equity-based framework. Because Part 31 is subject to the general principles of 49.201, we do not apply strict cost accounting principles here. "The use of business judgment, as distinguished from strict accounting principles, is the heart of a settlement." *FAR* 49.201(a). We cannot ignore equitable considerations and reasonable business judgment in our deliberations.[5]

Still, plaintiffs bear the burden of proving their termination for convenience damages. *See Lisbon Contractors, Inc. v. United States*, 828 F.2d 759, 767 (Fed. Cir. 1987); FAR 31.201-3(a); *see also Bath Iron Works Corp. v. United States*, 34 Fed. Cl. 218, 231 (1995), *aff'd*,98 F.3d 1357 (Fed. Cir. 1996). The costs considered in a termination for convenience recovery must also satisfy the general requirements of FAR Part 31-that the costs be reasonable, allowable and allocable. *See FAR* 49.113; *see also FAR* 31.201-2 to 31.201-4 (outlining the requirements of allowability, reasonableness, allocability, respectively); 31.205-42

[5] At the same time, we cannot fault Mr. Miller's emphasis on FAR Part 31. He is a cost accountant, and he carried out the mission that he was given. He did not have the access that he needed, and he was not provided other necessary tools as plaintiffs generally claim.

(providing cost principles "peculiar" to termination situations).

Overall Lack of Evidence that Plaintiffs "Padded" their Costs

Defendant had little evidence that plaintiffs attempted to inflate their costs. One would expect to find some improper charges claimed through inadvertence or negligence, if nothing else. But generally we were not provided with evidence of inflated costs claims through bad faith, negligence, or otherwise.[6] Most of plaintiffs' costs were incurred during a time when they had no reason to think that the costs would be reimbursed.

This opinion will show that for the most part, we found no basis for questioning the reasonableness, allowability, or allocability of plaintiffs' claimed costs.

DISCUSSION

I. SUBCONTRACTOR SETTLEMENTS

FAR 49.104 provides, in pertinent part:

[6] As General Dynamics argues in its post-trial brief:

> "The fixed-price nature of the contract provided the contractors with a financial incentive during performance to incur only necessary costs, and to control strictly the amount of those costs.... And, because the contract was terminated for default, the contractors were liable, with no assurance of being reimbursed, for all the amounts they incurred after termination, including all of the amounts they paid to settle with their subcontractors."

Testimony at trial supported this argument.

> After receipt of the notice of termination, the contractor shall comply with the notice and the termination clause of the contract, except as otherwise directed by the TCO. The notice and clause applicable to convenience terminations generally require that the contractor-
>
> ....
>
> (g) Settle outstanding liabilities and proposals arising out of termination of subcontracts, obtaining any approvals or ratifications required by the TCO....

"Contractors shall settle with subcontractors in general conformity with the policies and principles relating to settlement of prime contracts in this subpart and subparts 49.2 or 49.3." *FAR* 49.108-3(a). "The use of business judgment, as distinguished from strict accounting principles, is the heart of a settlement." *FAR* 49.201(a). "The primary objective is to negotiate a settlement by agreement." *FAR* 49.201(b). "In appropriate cases, costs may be estimated, differences compromised, and doubtful questions settled by agreement." *FAR* 49.201(c).

Prime contractors must terminate all subcontracts related to the terminated portion of the prime contract and settle all liabilities and proposals arising out of termination of the subcontracts. *FAR* 49.104(b), (g). The A-12 contract entitles the contractors to the cost of settling and paying subcontractor termination proposals. *FAR* 52.249-2(f)(2)(ii). Such costs are "generally allowable." *FAR* 31.205-42(h); *FAR* 31.205-42(g)(1)(i)(B).

FAR 49.201 requires that the contractor be compensated fairly through the exercise of judgment. Cost and accounting data may be employed but are not rigid measures for determining fair compensation. Settlements may be executed on a "bottom line" basis. *See FAR* 49.201(b) ("The parties may agree upon a total amount to be paid the contractor without agreeing on or segregating the particular elements of costs or profit comprising this amount").

Contractors are entitled to the costs of subcontractor settlements provided the settlements are "arrived at in good faith, ... reasonable in amount, and ... allocable to the terminated portion of the contract." *FAR* 49.108-3(c). A settlement will be approved when it is the product of "arms-length bargaining, without collusion, and reflect[s] a sound exercise of prudent business judgment" by the prime contractor. *General Electric Co.*, ASBCA No. 24111, 82-1 BCA ¶ 15,725 at 77,806, 1982 WL 7083 (March 29, 1982), *aff'd* on recon., ASBCA No. 24111, 83-1 BCA ¶ 16,207, at 80,529, 1982 WL 7993 (December 1, 1982). The FAR does not encourage second-guessing of the exercise of business judgment. *Id.* at 77,804.

Subcontractor settlements may comprise the subcontractor's incurred costs, profit or loss adjustment, and the subcontractor's settlement expenses. If the sum is reasonable, allocable, and allowable, the subcontractor is entitled to recovery.

We ruled that defendant could not question plaintiffs' business judgment or negotiating tactics, but that it could submit evidence of investment, bad-

faith, self-dealing, or less than arms-length transactions. Defendant also could show evidence of willful neglect or wrongdoing attributable to the plaintiffs, if applicable.

A. Norden

Norden had a subcontract with General Dynamics to provide a radar system for the A-12. General Dynamics terminated Norden for default in April 1989, and Norden sued General Dynamics in June 1989. The parties settled this litigation in 1992 for approximately $40 million. As part of its termination settlement proposal to the Government, General Dynamics claimed the $40 million amount of settlement, $10 million in legal fees incurred in its defense, and $10.7 million in reprocurement costs.

We ruled in August 1997 that General Dynamics' decision to settle with Norden was made on the basis of sound business judgment. The Government argued that General Dynamics could not recover costs associated with the Norden settlement because it terminated Norden for default. Testimony at trial established that (1) General Dynamics faced a potential liability of $160 million; (2) a trial would have been litigated before a jury in Norden's home state of Connecticut; (3) security problems would have made trial dangerous and perhaps restrictive; and (4) Norden could have raised General Dynamics' own schedule slippage in its defense. General Dynamics determined that it was prudent to settle with Norden, and we declined to second-guess that reasoned decision. *See generally Nolan Brothers, Inc. v. United States*, 194 Ct. Cl. 1, 437 F.2d 1371, 1392

(1971) (holding that costs incurred as a result of a decision to terminate a subcontractor for default were recoverable so long as the decision was "one that a prudent business man would take in the circumstances").

B. Westinghouse

Westinghouse subcontracted with General Dynamics in 1988 to develop and supply the combined-function forward-looking infrared radar system for the A-12 aircraft. As a result of the Norden termination in 1989, the subcontract was superseded by a new subcontract requiring Westinghouse to develop and supply the multi-function radar systems also. Westinghouse began work on the new contract late in the development phase of the project. *See McDonnell Douglas Corp. v. United States*, No. 91-1204, 1997 WL 842408 (Fed. Cl. Aug. 21, 1997). The Government terminated the prime contract in January 1991, and General Dynamics terminated Westinghouse in April 1991. Westinghouse submitted a termination settlement proposal and request for equitable adjustment in May. The parties negotiated a $73 million settlement in August 1991. The Government challenges $51,099,249 of that settlement.[7]

[7] The Government challenged costs as either "questioned" or "pending." Questioned costs are considered by defendant not to be reasonable, allowable, or allocable. Costs are designated "pending" because the Government's audit team claims it did not have enough information about them to make an evaluation. We reviewed all challenged costs on the same basis.

1. Expedited Settlement

The Government argues that Westinghouse and General Dynamics colluded or engaged in less than arms-length dealing because of circumstances surrounding their settlement. That is, General Dynamics departed from its internal procedures and settled with Westinghouse on an expedited basis before an audit and claims analysis was performed. Defendant suspects that General Dynamics expedited settlement so that it could enlist Westinghouse's support in this litigation.

The Westinghouse settlement was allocable, allowable, and reasonable. That the settlement was achieved on an expedited basis does not taint its integrity. Settlement was made contingent upon a successful audit. General Dynamics settled with Westinghouse long before the prime contract termination was converted into one for convenience, and it faced severe litigation risk. General Dynamics had no incentive to settle with Westinghouse on a less than reasonable basis. Westinghouse sought $110 million; the parties settled for $73 million.

2. Combined Loss Ratio

Defendant challenges $27,573,468 due to an alleged improper calculation of Westinghouse's loss ratio. The loss ratio is impermissible, according to defendant, because unlike those applied to other subcontractor settlements, the loss ratio applied to Westinghouse combined FSED, Lot I, and Lot II. This had the effect of increasing Westinghouse's recovery and the Government's ultimate liability by $27,573,468. "The impact of combining the loss ratio

is to dilute the impact [of] the loss ratio on the FSED portion of the contract which represented 82% of the actual costs at termination," defendant argues.

General Dynamics states that it imposed a combined loss ratio here because the subcontract required it. Westinghouse subcontracted with General Dynamics initially to supply the combined-function forward-looking radar system only. After General Dynamics terminated Norden, its initial subcontractor, however, it assigned Westinghouse the additional responsibility of developing and supplying the multi-function radar system. In return for accepting the multi-function radar duties late in the development phase, Westinghouse demanded that any loss ratio imposed combine FSED, Lot I, and Lot II. Motorola was the only other subcontractor to extract such a concession. General Dynamics did not impose a combined loss ratio on Motorola because Motorola was not in a loss position at the time of termination.

Loss ratios were segregated for purposes of progress payments for more than a year after General Dynamics and Westinghouse renegotiated the subcontract, but Westinghouse insisted that they be integrated. General Dynamics' legal department agreed, and sought and obtained Government approval. The Government argues that it approved the combined loss ratio for progress payments only, not for final settlement. We are not aware that Government approval is required in such circumstances. Moreover, there is no prohibition against combining loss ratios. The application of a combined loss ratio to the Westinghouse subcontract does not demonstrate collusion or less than arms-length dealing.

General Dynamics believed that it was required to combine FSED, Lot I, and Lot II for purposes of assessing any loss ratios, and that position was not unreasonable. The contract does not limit the application of a combined loss ratio to progress payments only.

Moreover, Westinghouse demanded that loss ratios be combined as consideration for agreeing to perform the multi-function radar contract late in the program. The first subcontractor, Norden, was terminated more than a year into contract performance in 1989. Westinghouse's performance period was compressed. General Dynamics needed exceptional performance from Westinghouse, and got it. It was reasonable for General Dynamics to agree to a combined loss ratio.

3. Low Range Estimate at Completion Value

General Dynamics engineers generated a range of estimate at completion (EAC) values that settlement negotiators could employ to compute the loss ratio for the Westinghouse settlement. The values ranged from low to high and General Dynamics used a low value at settlement. Specifically, General Dynamics' engineers recommended a range of possible EACs from $163 million to $175 million. The negotiators actually used an EAC of $165.8 million. The Government contends that they should have used an EAC at the mid-point of the range. This would have increased the loss adjustment and reduced the Government's liability by $3,602,687. It was unreasonable for the contractor to select a lesser EAC value

within the estimated range, according to the Government.

General Dynamics derived the estimate at completion from a reasonable exercise of business judgment and consideration of other information in addition to engineering analysis. It weighed competing considerations and input from financial and business personnel. This exercise resulted in the departure from a mid-point in the estimated range.

That General Dynamics' negotiators employed a value from the low end of the range does not invalidate it. The FAR expressly permits a contractor to employ business judgment in reaching a settlement with the subcontractor. *See FAR* 49.201(a). Engineering was only one source of information that General Dynamics considered before selecting its EAC; it consulted business and financial personnel, and weighed competing considerations. This is the essence of the exercise of business judgment.

The Government's solution-arbitrarily to choose the mid-point of the engineering department's range-is not consistent with the exercise of business judgment. We find no support for the position that it is per se unreasonable for a contractor to select a value that is below the mid-point of an estimated EAC range.

4. Profit on Lots I and II

General Dynamics applied a loss ratio of 84.87% on Lot I progress payments prior to terminating Westinghouse. Lot II progress payments were suspended in December 1990. Defendant questions certain costs because General Dynamics settled with

Westinghouse allegedly on the basis of 15-20% profit margins. Defendant challenges $9,397,228 because it appears that General Dynamics credited Westinghouse with profit for Lots I and II while the contract was in a loss position. The Government argues that it was improper to pay Westinghouse profit. General Dynamics denies that it paid Westinghouse profit, but that instead it applied a combined loss ratio of 85.73% to the Westinghouse contract.

If the loss ratio is segregated, it may appear that Westinghouse received profit for Lots I and II. We stated that it was reasonable for General Dynamics to combine loss ratios in the circumstances of this case, however. The combined loss ratio precluded Westinghouse from making profits. The Government's argument assumes that General Dynamics was required to segregate loss ratios, but the contract did not require segregation.

5. Inventory Transfer

Upon termination of its sub-contract with General Dynamics, Westinghouse transferred inventory originally slated for use on A-12 to non-A-12 programs on a total cost basis. Westinghouse's termination settlement proposal, Form SF 1436, took into account Transferred Costs as well as Disposals and Other Credits. Westinghouse placed the transferred cost amount on line 16, which accounts for disposals and other credits, then applied a loss ratio to that amount.

The Government argues that the entire amount of transferred inventory should have been included in Disposals and Other Credits without taking into ac-

count the loss ratio. This would have further reduced the Government's liability.

DCAA Contract Audit Manual § 12-311 provides instruction as to the type of items included within the Disposals and Other Credits line on Form SF 1436. The section states in part:

> Credit amounts included in a settlement proposal normally represent (1) an offer by the contractor to purchase inventory at less than cost, (2) the proceeds from the sale of termination inventory, or (3) a combination of (1) and (2)....

Westinghouse transferred common items at full cost to a non-A-12 program. It did not offer to purchase or sell inventory. Thus, the cost of the transferred inventory should not be included at all on line 16 (Disposals and Other Credits). The plain language of DCAM § 12-311 suggests that the Government's interpretation is incorrect.

Westinghouse transferred common items for other uses as instructed by *FAR* 31.205-42 and *FAR* 45.606-2. Although Westinghouse included the transferred costs of the inventory under Disposals and Other Credits on Line 16, it applied a loss ratio to the costs. This has the same effect as if Westinghouse had included the costs on Line 7 (Transferred Costs), then applied the loss ratio to the remainder. While it would have been proper to include the entire amount of transferred costs on the transferred cost line, thereby reducing total costs before applying the loss ratio, Westinghouse essentially removed those transferred costs from the settlement equation by

applying a loss ratio to them on the Disposals and Other Credits line.

Moreover, according to DCAA's training manual (Audit of Terminated Contracts, FAO Training Course 2211), removal of common items from program costs prior to applying a loss ratio is required. While Westinghouse did place the transferred cost amount on the Disposals and Other Credits line, it essentially took the cost of those transferred items out of the settlement proposal by applying the loss ratio to them. The Government's liability remains the same.

6. Consideration of REAs

Westinghouse submitted requests for equitable adjustments totaling $44.5 million as part of its termination settlement proposal. General Dynamics settled those claims for $11 million, but it did not determine who was responsible for the adjustment. General Dynamics did not verify that REAs paid to Westinghouse arose solely because of government fault, but paid the REAs and claimed $10 million as part of its termination settlement proposal. Defendant contends that it cannot be held liable for such claims when General Dynamics does not prove that government conduct or inaction caused the adjustment. The Government challenges $10,098,968[8] of the settlement as "pending."

[8] The Government determined that the impact of agreeing to pay Westinghouse $11 million in REAs is $10,098,968, after recomputing segregated loss ratios. We stated that Westinghouse was entitled to a combined loss ratio, so the Government's figure is incorrect. As we did not sustain this challenge,

This argument is essentially a reiteration of a government motion that we denied earlier. We stated before trial that the court would "consider the reasonableness of challenged subcontractor REA payments on the same basis as other costs allegedly incurred." McDonnell Douglas Corp. v. United States, No. 91-1204, at 2 (Fed. Cl. June 13, 1997) (denying defendant's motion for pre-trial determination that plaintiffs cannot recover amounts claimed for their subcontractors' requests for equitable adjustment). Costs are reasonable so long as they do not result from plaintiff's willful neglect or wrongdoing. Id. at 1. Settlements must be negotiated in good faith and incorporate the exercise of business judgment.

Westinghouse sought equitable adjustments totaling $44.5 million. General Dynamics obtained advice and assistance from technical, financial, and legal representatives before settling these claims. Engineers for General Dynamics reviewed the requests for equitable adjustments and determined that Westinghouse was entitled to an adjustment ranging from $12 million to $18 million. General Dynamics' lawyers proposed a range of adjustment from $9 million to $11 million. The actual $10 million adjustment incorporated the exercise of business judgment. Defendant has not shown that plaintiff's willful neglect or wrongdoing prompted the claims; nor is there a hint of bad faith.

however, we need not determine the actual impact of the payment.

C. Other Subcontract Challenges

We do not reprise the legal standards described in rulings above concerning Norden and Westinghouse. It is sufficient to state that no credible evidence of bad faith, willful neglect, or wrongdoing has been presented with respect to any of the following subcontracts: General Electric Aircraft Engines, Allied-Signal-Torrance; Allied Signal-Teterboro; SJ & LA-Hughes; Harris Corporation; SCI Technology, Inc.; Litton Systems; Sundstrand Aerospace; Menasco Aerospace; and Parker Hannifin. McDonnell Douglas' claimed incurred costs with respect to these subcontracts may be awarded, as they are reasonable, allowable and allocable. Plaintiff General Dynamics' claimed incurred costs with respect to Litton Amecon; GE-Utica; Martin Marietta; Models and Tools; Teledyne Ryan; Hewlett Packard; Motorola; Arkwin; Struthers Dunn; Parker Hannifin; and Hexcel also are reasonable, allocable, and allowable.

II. SUBCONTRACTOR REQUESTS FOR EQUITABLE ADJUSTMENTS

The Government challenges various subcontractors' requests for equitable adjustments, because "it is now uncontroverted that neither General Dynamics [n]or McDonnell Douglas even attempted to establish Government liability for the REAs." We stated in June 1997 that the court would "consider the reasonableness of challenged subcontractor REA payments on the same basis as other costs allegedly incurred." Plaintiffs exercised sound business judgment with regard to paying REAs to subcontractors. A court should not second-guess contractors who

make reasoned decisions in such circumstances, as noted above. Such costs claimed by plaintiffs are reasonable, allocable, and allowable.

We have even less reason to question plaintiffs' costs with respect to requests for equitable adjustments in this area than in the Westinghouse situation, given the evidence presented. The Government argues that "there is a requirement that a prime contractor evaluate a subcontractor claim to determine Government liability." If so, this is not a case in which the plaintiffs blindly passed on a claim for costs by the subcontractor to the Government. We see no compelling reason for subcontractors' requests for equitable adjustments to be treated differently from other subcontractor settlement costs. *See FAR* 49.201(b) ("The parties may agree upon a total amount to be paid the contractor without agreeing on or segregating the particular elements of costs or profit comprising this amount"). As Allen Broesche, a witness for General Dynamics, testified: "It was our money, and we reached a reasonable settlement." Plaintiffs had no expectation that any of these expenses would be reimbursed by the Government while negotiating with subcontractors over REAs or any other settlement expenses. We cannot disallow these costs.

III. DIRECT MATERIAL

[T]he audit team performed audit procedures, including sampling, to evaluate the allowability, allocability, and reasonableness of the [General Dynamics] and [McDonnell Douglas] direct material line (Line 1) items in their January 1994 Update.

These procedures were supplemented by Coopers' review of the February 1997 Update, and, as a result, Coopers questioned a total of $14,955,000 in MDC direct material costs ... and $53,143,152 of GD's proposed direct material costs. Additionally, Coopers categorized $9,935,196 as pending for MDC due to MDC's failure to perform a commonality study. In general, the questioned direct material costs include overpayments to vendors, defective items that were returned and not properly credited, items actually used or usable for other programs, excess purchases, purchases incurred long before required, and inadequate or sloppy documentation.

A. General Dynamics-Direct Material

1. Sample Testing of General Dynamics' Costs

Coopers & Lybrand's audit team "reviewed documentation to verify necessity, cost, payment, receipt, physical existence, and disposition." Mr. Miller testified that General Dynamics did not provide the audit team with appropriate termination inventory schedules. Robert Wright[9] generally agreed that General Dynamics' inventory schedules were not available. According to Defendant, General Dynamics' 'accounting system' was incapable of providing the audit team with termination inventory schedules, as re-

[9] Wright had primary responsibility for the preparation of General Dynamics' termination for convenience claim. A long-time employee of General Dynamics in the financial cost accounting area, he had served as the deputy program director of business management for the A-12 program since 1984. Allen Broesche, John Lamers, and Ron Hancock also had worked on the A-12 program during performance of the contract.

quired by the FAR, which would have identified the current physical location and estimated costs of material that GD purchased from vendors. As a result, the audit team used an accounts payable system and statistically selected transactions for further testing.

Using audit sampling procedures, the audit team selected for review 47 items by vendor and purchase order number. Mr. Miller testified that in developing the sample to be tested, the audit team received technical assistance from the DCAA office in Memphis, Tennessee. After testing the "sampled items," the audit team met with General Dynamics personnel to seek additional explanation or further documentation as appropriate. After evaluating the responses the audit team either would withdraw the preliminary exceptions or leave them in place, depending on the documentation available.

"Dollar unit sampling" focuses on the dollars in a given accounting population. The audit team used this method for review of General Dynamics' incurred direct costs. According to the DCAA Contract Audit Manual, dollar unit sampling is a valid technique to account for the reasonableness of costs incurred for direct material. *See* DCAM B-503.1. We agree with the Government that audit sampling is recognized by the accounting and auditing profession as being a proper and appropriate method for review.

Miller testified that in dollar unit sampling "you're not looking at every dollar in the population, you're only looking at certain dollars in the population, but those are representative and will be representative of the rest of the population." When errors

in the sample population are found, an error proportion is calculated and used to determine the extrapolation percentage. "Of approximately 22 million [dollars] reviewed, Coopers identified $6.36 million of questioned costs within the sample. Using dollar unit sampling procedures, Coopers projects the total amount of questioned direct material costs to be approximately $53,143,152."

While we recognize that the audit team's methods applied proper sampling techniques, we do not agree with all of their findings and extrapolations. Mr. Miller questioned many direct costs incurred on the grounds of allocability and allowability. Where sufficient evidence of allowability, allocability and reasonableness of costs are found, however, the court must sustain those costs as incurred.

2. Lack of Documentation

a. Bell Helicopter

General Dynamics purchased a tool for the wing-fold of the A-12 from Bell Helicopter. Defendant claims that General Dynamics paid Bell Helicopter "over and above the price listed in the purchase order reviewed." The audit team questioned $2,671 of $23,055 paid to Bell Helicopter because it was not satisfied that General Dynamics' documentation supported the costs claimed. General Dynamics explained that it "could not locate the change order that would have explained the precise reason for the second of two increases in the purchase price of the tool, which increased the price from $20,384 to $23,055." The audit team extrapolated a challenge of $885,135 in costs from the $2,671 figure.

Other documentation supports General Dynamics' position. It paid Bell Helicopter $23,055 pursuant to an invoice for the manufacture of an A-12 tool. Before issuing a check to Bell Helicopter, General Dynamics' accounts payable clerk made a notation on the check indicating that she had verified the invoice amount against the final purchase order amount that had been entered by the buyer in the procurement file. Mr. Miller acknowledged the existence of documentation indicating that the change was for "rework." General Dynamics contends that it is common for rework to be done during the manufacture of tools developed for a RDT & E; here there is no dispute that Bell Helicopter was providing tooling work.

The court's role is to determine whether General Dynamics incurred the cost, whether it did so for the A-12 contract, and whether it did so for a legitimate purpose. Although Mr. Miller did not find these factors sufficient to document the increased cost, evidence presented at trial satisfied the court that the entire cost was allowable, allocable and reasonable. *See, e.g., FAR* 49.201(c).

b. Cohn and Gregory

The audit team challenges the entire $7,714 the General Dynamics paid to Cohn & Gregory for PVC piping and valves. After extrapolation, this becomes a challenge of $7,640,132.

The audit team sought a "requirements listing" to determine whether the items purchased from Cohn & Gregory were required for the A-12. General Dynamics provided no such list, but submitted the dec-

laration of an employee, Steve Wells. Mr. Miller testified that this representation was not sufficient to make a determination of allowability, allocability, or reasonableness. General Dynamics acknowledged that it could not produce much documentation other than the declaration. However, Mr. Wright testified that the PVC pipes and valves were purchased for an environmental control test stand for the A-12. Mr. Wells was the buyer of the material. His declaration stated that "[t]he fittings and other hardware was purchased to build the test setup shown in the drawings." An invoice from Cohn & Gregory, signed by Wells, contains a unique A-12 work order number. This cost is properly awardable.

c. Fiber-Resin Corporation

General Dynamics claims costs for tooling foam boards that were shipped to Cadillac Motor Car Division as furnished material to be used to manufacture a tool for A-12 (Tool # R15649). Coopers questioned $30,774 associated with this item for lack of documentation "and an inability on the part of GD to demonstrate the use, location, or disposition of this material." Cadillac was not a General Dynamics A-12 vendor, but it was a vendor to Models & Tools, an A-12 subcontractor. Using its sampling technique, Coopers & Lybrand extrapolated a challenge of $7,640,132 from the $30,774 questioned item.

Mr. Miller testified that General Dynamics did not provide sufficient documentation to support this cost item. Coopers & Lybrand reviewed an internal General Dynamics audit of Models & Tools and found that General Dynamics' own analysis con-

cluded that Models & Tools' cost accounting system was inadequate. The cost accounting system failed to identify the tooling foam boards, for example.

Payment was made to Fiber-Resin, the producer of the foam board, while the board was shipped to Cadillac. The type of foam board ordered is consumed during the production of a tool. After termination, General Dynamics issued an abandonment certificate to Models & Tools for Tool # R15649. This indicates that the tool, which was classified as work-in-process, had no value. DCAM 2-202(a) provides that because "audits frequently require a wide variety of skills, an auditor may need technical assistance from other disciplines such as legal, engineering, and production/quality control. The auditor should make arrangements to secure any needed technical assistance from the ACO/plant representative or responsible acquisition agency." General Dynamics argues that Miller should have sought technical assistance in such a circumstance.

Plaintiff's documentary evidence and its testimony concerning consumption of the foam board material justify award of its costs.

3. "Expediting Charges"

Coopers questioned certain of General Dynamics' direct material costs because General Dynamics paid premium prices for expediting delivery of items "long before they were actually required by GD." The Government points out that many of the materials in issue still were on hand when the contract was terminated.

a. Stanley Aviation

The audit team challenged $70,077 in expediting charges paid to Stanley Aviation for providing parts for the A-12 full-scale mock-up. Miller questioned this amount at trial "due to the fact that the item was not used at termination, yet it had been expedited earlier." The sampling technique here creates a $6,626,207 challenge.

The minutes of a meeting of the General Dynamics "Procurement Ad Hoc Committee" on September 21, 1989 include the following entry concerning the Stanley Aviation order: "*Schedule*: The A-12 program schedule dictates the requirement for procurement to initiate an expediting fee to authorize the supplier to perform to an expedited schedule that supports the A-12 program needs." According to General Dynamics, "the parts still were on hand at termination because the A-12 delivery schedule was extended by 18 months in 1990, *after* these parts were ordered." The full-scale mock-up was affected by this schedule change.

The Government did not establish that *when the purchase order was placed* with Stanley Aviation, General Dynamics should have known it did not need to expedite delivery. General Dynamics points out that this is another area in which Miller could have benefited from technical and contract assistance. *See* DCAM 2-202(a).[10]

[10] Mr. Miller acknowledged, for example, that he did not know the first flight date. He maintained that he did not necessarily need to know anything about the contract schedule to challenge a cost related to an expediting charge.

General Dynamics made a reasonable business judgment at the time the purchase order was made. The fixed-price nature of the contract and the attendant cost risks undertaken by General Dynamics, along with credible testimony at trial that General Dynamics did not make the decision to incur expediting charges lightly, support this conclusion. *See, e.g., Boeing Aerospace Operations, Inc.*, ASBCA Nos. 46274, 46275, 94-2 BCA ¶ 26,802, at 133,282, 1994 WL 96970 (March 21, 1994) (reasonableness is judged by considering "all of the relevant circumstances existing at the time of the incurrence of the costs") (citing *FAR* 31.201-3), *aff'd on recons.*, ASBCA Nos. 46274, 46275, 94-3 BCA ¶ 27,281 at 135,908, 1994 WL 651887 (November 9, 1994).

b. Standard Pressed Steel & Kamatics

Coopers & Lybrand challenges $3,007 in expediting charges to Standard Pressed Steel-extrapolated to arrive at a $2,792,498 challenge. The entire amount of a $2,059 acquisition of ball bearings from Kamatics is questioned as well. This amount is increased to a challenge of $7,640,132. Mr. Wright testified that in both of these situations, "expediting was done to meet a schedule of a subassembly, an indentured-type system for manufacturing." As mentioned above, General Dynamics had to consider carefully any decision to incur expediting charges. The charges incurred here are properly awardable.

4. Other Direct Material Challenges

a. Sierra Alloys

Coopers & Lybrand challenges $220,924 of a $421,764 purchase of 42 pieces of titanium from Si-

erra Alloys, to be used for the inner wing engine bay doors and the inner wing. The audit team could account for only 20 of the 42 pieces at termination, and it challenged the cost of the other 22 pieces. The $220,924 challenge is extrapolated to $4,001,974.

According to General Dynamics, even if 22 of the pieces somehow were "lost," its termination claim should be reduced only by the fair market (salvage) value of those 22 pieces. *See FAR* 49.204 and DCAM 12-304.10 (with respect to termination inventory that is undeliverable to the government because it was damaged, destroyed, or lost, the fair value of such undeliverable material should be deducted from the termination settlement proposal). General Dynamics points out that proceeds from the sale of 12 pieces of scrap garnered $ 17,765-approximately $1,480 each. Applying this average price to the 22 "lost" pieces, the value of the challenged pieces totals $32,560.

We find that a $32,560 deduction is appropriate because that is the fair value of the lost material. Extrapolating from that figure, we deduct $589,815 from plaintiffs' claim.

b. Stewart-Warner

This challenge is to $36,315 of a $435,780 purchase of 12 instrument landing systems from Stewart-Warner. The audit team could account for only 11 of the 12 items at termination, so it challenged the entire acquisition cost of the twelfth item. Using its sampling methodology, the audit team extrapolates a challenge of $636,678.

General Dynamics argued that because records were available for the other eleven items, it should

be entitled to a credit because "all parts have been accounted for." The Government contends, that "[t]he fact that GD was able to provide adequate documentation regarding the eleven that went to salvage suggests that the twelfth was not salvaged."

General Dynamics ordered, received, and paid for 12 items for use on the A-12 contract. It rejected one of the 12 items and returned it to the vendor. The vendor later shipped the twelfth item directly to the A-12 manufacturing facility in Tulsa, Oklahoma. General Dynamics attempted to return the items to Stewart-Warner after the contract was terminated, but Stewart-Warner refused to accept them. General Dynamics salvaged eleven of the items for little value. We have no documentation concerning disposition of the twelfth item, but these facts are not in dispute.

General Dynamics argues that "it is reasonable to rely on the termination procedures established by the contractors, which reasonably attempted to account for and dispose of all A-12 inventory." It notes further that the contract had been terminated for default, so "at the time GD disposed of the A-12 inventory it had no guarantee it ever would recover its incurred costs, and the company thus had an obvious incentive to dispose of its inventory in a manner that would recover as much of the cost of the item as possible."

We cannot find sufficient grounds for awarding the value of the twelfth item as an incurred cost. As mentioned above in the Stewart-Warner context, the FAR and DCAM contemplate that when inventory is

lost, the fair value of that material should be deducted from the termination settlement proposal. That could be accomplished here by considering the value of the eleven items sold for salvage to arrive at a value for each item, and then applying that value to the twelfth item. We did not hear evidence of the salvage value of those items, other than testimony that they had very little value. We therefore cannot impute a salvage value to the twelfth part, and instead must deduct the acquisition cost of the twelfth item from General Dynamics' proposal. This method is consistent with the Government's challenge. We therefore sustain the extrapolated challenge argued by the Government, $636,678.

c. Universal Alloy

Coopers questions certain costs for materials in excess of the requirements of the A-12 FSED contract and Lots I and II options. For example, GD purchased aluminum from Universal Alloy for use on various programs, including the A-12. GD originally charged the costs of a small portion, only 24 feet, to the A-12 contract; in fact, the purchasing document specifically stated that the remainder of the aluminum was for "various prime contracts." However, more than two years after termination, GD charged an additional 262 feet of the aluminum to A-12. As there is no evidence that the A-12 program required aluminum in excess of 24 feet, Coopers questions all costs for aluminum in excess of that amount.

The challenge based upon these costs is $7,640,132-extrapolated from an initial figure of $1,670.

We are persuaded that allocation to the A-12 contract was reasonable. *FAR* 31.205-42(a) defines common items as those "reasonably usable on the contractor's other work." Testimony from Mr. Wright indicates that although some aluminum may have been available for use on other programs if needed, no such need developed. The aluminum had been acquired originally for the A-12 program. Because the aluminum did not prove to be useful on another program, General Dynamics transferred an additional 262 feet of aluminum (at a cost of $1,670) into the A-12 program on February 13, 1993. At the time of the transfer, the contract was considered to be in default. Thus General Dynamics had no incentive to transfer the costs to A-12 when reimbursement by the Government was unlikely. We find that this cost is properly awardable to General Dynamics.

d. Voi-Shan Manufacturing

Defendant challenges a $1,902 purchase of 46 bolts from Voi-Shan Manufacturing-extrapolated to arrive at a challenge of $7,640,132. Defendant's position is that these items should have been returned to the manufacturer, likely for full credit.

Plaintiff points out that FAR 45.605-2 permits a contractor to recover from the Government a restocking charge of up to 25% of the cost of the returned items, as well as transportation and handling costs associated with the return. *See also* DCAM 12-304.8 ("The contractor may not include the cost of returned

property in the settlement proposal but may include the transportation, handling, and restocking charges for the returned property"). Mr. Miller conceded that the cost of returning the bolts may have met or exceeded the entire $1,900 purchase price.

General Dynamics judgment not to return the bolts was sound, given the doubtful economic value of returning them.

B. McDonnell Douglas-Direct Material

The Government divides McDonnell Douglas' direct material costs into three categories: (1) contractor furnished equipment; (2) subcontract costs; and (3) manufacturing material. In reviewing McDonnell Douglas' claimed direct material costs, the audit team tested the "control, physical existence, and disposition or termination inventory on hand at the time of the audit."

Unlike General Dynamics' accounting system, McDonnell Douglas' records permitted the audit team to review incurred direct costs through non-statistical sampling means:

> MDC's records permitted the Audit Team to conduct physical inventory verification testing with regard to termination inventory on hand in August 1994. Mr. Miller testified that, as a result of these procedures, the Audit Team found discrepancies in quantity, description, or location in nearly one-third of the 76 items that the Audit Team selected for verification. Coopers could not project the results of this sample to the entire

population because MDC did not provide priced inventory schedules. Therefore, Coopers questions only $75,042, which represents the specific items quantified.

Physical inventory verification testing is a proper sampling method. If sufficient evidence sustains a claimed cost, however, the cost should be awarded.

1. Damaged and Defective Inventory

The Government asserts that after the physical inventory procedures, McDonnell Douglas supplied documentation as to the location of several missing "CFE/major subcontracts items selected for physical inventory." McDonnell Douglas had also returned certain of these items to its vendors or labeled them as defective, damaged or rework items. According to the Government, "[McDonnell Douglas] provided no satisfactory evidence that it took credit for these damaged or defective components as a part of the subcontractor settlement process and, accordingly Coopers questions $1,439,405 in associated costs."

Mr. Hancock testified that the costs to repair such items were added to increase subcontractors' estimates at completion. This would have the effect of reducing the subcontractors' recovery. On the record before the court, we cannot say that these costs are unreasonable.

2. Common Inventory

The Government also contends that during physical inventory testing, the Defense Plant Representative Officer's technical representatives identified material that could be used on other programs. "The

costs of items reasonably usable on the contractor's other work shall not be allowable unless the contractor submits evidence that the items could not be retained at cost without sustaining a loss." *FAR* 31.205-42(a). Additionally, "[a]ny acceptance of common items as allocable to the terminated portion of the contract should be limited to the extent that the quantities of such items on hand, in transit, and on order are in excess of the reasonable quantitative requirements of other work." Id. Additional procedures were performed by the Coopers & Lybrand audit team "to identify amounts of termination stores material that MDC actually used in other programs and, in some cases, purchased from vendors after termination." Based on these procedures, the Government questions a total of $764,282 as "common inventory" because the costs claimed may not be included in termination costs if the inventory could be used on other programs, as alleged here.

Mr. Miller acknowledged that the contracting officer should make a determination whether inventory is common, but that the Government did not do so in this case. He further acknowledged that the Government did not provide an inventory verification report, did not appoint a plant-wide clearance officer, and did not make an assessment of commonality at the time of termination. He stated that with respect to post-termination inventory, the Government's position was that "they wouldn't do anything in terms of dealing with the contractors on inventory, other than to let them know that there had been a termination for default." [11] He stated that "in general, my

[11] *See supra* note 1.

understanding is that they didn't get involved or want to be involved in that particular process because it was a termination for default." Mr. Hancock testified that all of the direct material costs in the company's claim were in excess of its needs. He detailed McDonnell Douglas' procedure for transferring common items. We cannot question McDonnell Douglas' claims in this area.

3. Panstock Cost Transfer

The audit team conducted a review of pre- and post-termination journal vouchers, and discovered a February 22, 1991 entry allocating $2,611,179 of panstock to the A-12 program. The Miller report questions the $2,611,179 as a common item unallowable under *FAR* 31.205-42.

As McDonnell Douglas uses the term, panstock describes low-value, high volume material. Michael Cromer[12] testified that panstock can be either common and used for multiple programs, or unique and used on a single program.

Hancock and Cromer testified that McDonnell Douglas systematically moved panstock and other inventory to other programs where it could, and that its incurred costs do not include any "common items," for which the Government is entitled to credit under *FAR* 31.205-42(a). In short, McDonnell Douglas sought to mitigate its costs related to panstock.

Panstock should not be treated differently from any other cost challenged as a common item.

[12] Mr. Cromer was McDonnell Douglas' manager of government accounting.

McDonnell Douglas tried to limit the amount of panstock attributable to the A-12 contract by attempting to find a use for it on other contracts. The remaining A-12 panstock exceeds McDonnell Douglas' needs; it remains a cost to which McDonnell Douglas is entitled.

4. Fixtures Loaned to Other Programs

The Government maintains that Coopers identified six significant test fixtures of physical inventory that reportedly were being used on other McDonnell Douglas programs. The costs for these items, however, remained in McDonnell Douglas' January 1994 termination settlement proposal update. According to the Government, "McDonnell Douglas would not quantify the costs of the fixtures prior to Coopers' issuance of its May 8, 1995 incurred cost audit report." After the incurred costs audit report was issued, the Government learned through discovery that McDonnell Douglas had "quantified the costs of five of the test fixtures at $10,065,599." Coopers questioned this entire amount.

Special test equipment is an allowable and recoverable A-12 contract cost under *FAR* 31.205-40. Mr. Miller admitted that the six test fixtures were built specifically for the A-12 contract. Miller argued that the costs nevertheless should be recovered under other contracts because the test equipment had been loaned occasionally after termination. In McDonnell Douglas' view, this simply mitigated costs to the Government. McDonnell Douglas points out that "no contracting officer on any other program has agreed to accept or pay any portion of the costs of the special

test equipment." It concludes based on the foregoing that there is no basis to disallow this $10,066,000 in special test equipment costs under *FAR* 31.205-40. To do so would mean that it "could not recover its incurred costs under the A-12 or any other contract."

We agree. These costs are awardable to McDonnell Douglas.

C. Other Costs-General Dynamics and McDonnell Douglas

1. Unabsorbed Overhead

The Government argues that McDonnell Douglas cannot recover unabsorbed overhead costs:

> Coopers identified and questioned $12,538,718 in costs transferred, after termination of the prime contract, from overhead pools to the Termination Proposal. These costs were for facilities and were charged to overhead pools during the performance of the A-12 contract. However, after termination MDC attempted to charge these costs specifically to the A-12 contract, even though prior to January 8, 1991, other contracts absorbed these costs pursuant to MDC's overhead allocation policies. Neither Mr. Hancock nor Mr. Cromer, the two witnesses proffered by MDC to testify to this issue could explain why the accounting basis of the treatment of these overhead costs was different after termination than before. Significantly, MDC presented no expert evidence to rebut Mr. Miller's testimony that the costs in

> question were "by their very nature, overhead costs." Indeed, MDC questioned these same types of costs in settling with its subcontractor, SJ & LA Hughes.

These alleged costs were, in actuality, claims for unabsorbed overhead, inasmuch as they represented overhead costs that MDC allegedly could not be [sic] recover, using the post A-12 business base for allocating its overhead costs. As such, the law proscribes their recovery in a termination for convenience. *See* DCAAM ¶ 12-305.7(b)-(c); F. Alston, M. Worthington, & L. Goldsman, CONTRACTING WITH THE FEDERAL GOVERNMENT 360-61 (3d ed.1992). [13]

McDonnell Douglas disputes the Government's characterization of this expense as unrecoverable unabsorbed overhead. Mr. Cromer testified that the $12,539,000 amount was specific to the A-12 contract and that it represented the cost of idled A-12 facilities accounted for exactly as DCAA has required on two other terminated contracts.

The issue is whether it was proper for McDonnell Douglas to remove such costs from the company's overhead pools, and include them in the termination proposal as incurred for the A-12 program.[14]

[13] Cf. P. Trueger, ACCOUNTING GUIDE FOR GOVERNMENT CONTRACTS (10th ed.1991) 713.25 (discussing court and board cases on recovery of unabsorbed overhead).

[14] The Government pressed Cromer on cross to explain why the $12.6 million in costs were transferred:

> Q: Okay. And prior to the termination of the A-12 contract, where were those costs reflected?

Cromer and Hancock testified that the idle facility costs were specific to the A-12 contract, but were charged to overhead pools until termination. According to Cromer, the practice of assigning depreciation into an overhead pool-without regard to whether it was a program-specific asset or a general administrative cost-was standard for McDonnell Douglas. In

> A: They were reflected in capital assets and then the depreciation went into overhead.
>
> Q: So those costs were allocated among all contracts at McDonnell Douglas, or at least government contracts, including the A-12, right?
>
> A: That is correct.
>
> ....
>
> Q: Can you explain why you decided to move the costs out of the overhead pools to the A-12 termination?
>
> A: Because that was our policy at McDonnell Aircraft Company relative to assets that related to a terminated contract.
>
> Q: Can you tell me why you did it, though? I mean, theoretically, what was the underpinning of that decision?
>
> A: The basis for that was that these assets were acquired for a particular program, and they were capitalized and depreciated. And when a program was terminated, it is part of the cost associated with that program. I guess that's basically all I can describe it as.
>
> Q: But you would agree with me, sir, that prior to the termination, even though the assets had been acquired for a specific program, you were recovering those costs by charging them to all contracts, A-12 and others?
>
> A: They were included in the depreciation and the overhead expenses, yes, sir.

other words, the fact that an asset was in an overhead pool did not necessarily identify that asset as a general, administrative type of asset. Mr. Hancock testified that McDonnell Douglas attempted to find alternative uses for the facilities that were specific to A-12. He stated that after the facilities remained idle for some time, however, "we decided that we would claim these costs."

Mr. Cromer testified that claiming these costs in the A-12 termination proposal was not an aberration. He described two prior incidences of adjusting overhead depreciation pools following a convenience termination. Cromer testified that after the Tacit Rainbow Program was terminated for convenience, the DCAA "specified in their audit report that it should be charged directly to the termination claim." Similarly, with respect to the Atlas program, costs in the overhead pool were "moved from the overhead pool and charged directly to the termination claim on the Atlas program."

These assets were program-specific; their costs were incurred in performing the A-12 contract. Asset costs assigned to overhead pools nevertheless can be program-specific, and included in a cost proposal associated with the termination of that program. Based on its prior experience with the DCAA, McDonnell Douglas sought to recover incurred costs inextricably associated with the A-12 program. We find that these costs are reasonable, allowable, and allocable.

2. Material Handling Expense

Coopers and Lybrand questioned $6,700,000 in material handling expense charges at General Dy-

namics related to unliquidated progress payments. Material handling charges are incurred when material is handled as it arrives. According to defendant, General Dynamics is "attempting to charge the Government for costs that were not and could not possibly have been incurred."

The base used to calculate its material handling expenses includes the amount of unliquidated progress payments paid by General Dynamics to its subcontractors. Mr. Miller testified that he challenged these costs because "they were payments included in the termination for convenience proposal for material handling expenses, overhead expenses for material handling, that were applied to progress payments that didn't represent deliveries and shipments."

General Dynamics notes that the costs related to material handling are principally labor, such as "the costs of paying people to move items in and out of warehouses and to help procure material."[15]

[15] General Dynamics provides the following additional explanation in its post-trial brief:

> At GD's Ft. Worth division, a pool of people at one end of the factory waited to receive material, which would pass through inspection and be delivered to the place on the factory floor where it was needed. These expenses were incurred whether or not material was being handled. GD divided the expenses for this labor between the various contracts at the Ft. Worth division. To divide the costs between the contracts, a "base" was established, and a rate that was negotiated with the ACO was applied to the base to determine the amount to be charged to each contract. The base that GD used for all of its contracts, including the A-12, included both liquidated and unliquidated progress payments. GD had

We find that the material handling costs noted by General Dynamics were incurred. It had used the same accounting system before with Government approval. The system provided a method whereby General Dynamics could allocate material handling costs to different contracts, thus accounting for A-12 expenditures properly. General Dynamic's accounting system was not unreasonable. We see no reason to impose a new allocation method upon plaintiff retroactively. *See Litton Systems, Inc. v. United States*, 196 Ct. Cl. 133, 449 F.2d 392, 399 (1971).

used this method for years, with disclosure to, and approval by, the government.

....

Nevertheless, [Coopers] challenges the use of this method because it appears to allow GD to recover material handling on materials represented by unliquidated progress payments that were never handled. This challenge ignores the fact that the base is merely a method to estimate the proper allocation of actually incurred overhead between various contracts. The challenge in fact would have the effect of denying GD reimbursement of material handling expenses actually incurred. Because GD with full knowledge and approval of the government divided its pool of costs among its various contracts using a calculation that included unliquidated progress payments, removal of those payments from the A-12 base after the fact would result in underestimating the A-12 contract's pro rata share of those actually incurred expenses. The government cannot retract retroactively its approval of a contractor's established accounting method to the detriment of the contractor. *See Litton Systems, Inc. v. United States*, 196 Ct. Cl. 133, 449 F.2d 392, 394, 399-401 (1971).

3. Excessive Overtime

a. General Dynamics

Coopers listed as pending $3,829,421 of General Dynamics' overtime expenses because the company apparently could not explain adequately why it experienced overtime hours in excess of that estimated in its Best and Final Offer.

No legal authority mandates that overtime cannot exceed the target estimates made in a BAFO. This was an incentive contract. Plaintiffs point out that Mr. Miller lacked the technical expertise to appreciate the need for significant overtime in General Dynamics' performance of the contract. See DCAM 2-202(a).

The standard that we employ to determine the awardability of the overtime expenses claimed here is whether they are allowable, allocable, and reasonable. *See, e.g., Worsham Constr. Co, ASBCA No.25907*, 85-2 BCA ¶ 18,016, at 90,369, 1985 WL 16693 (March 22, 1985). Testimony at trial established that the overtime was incurred in performance of the A-12 contract. The overtime did not exceed an amount that would have been incurred by a prudent business person, and therefore is allowable. *See, e.g., FAR* 31.201-2, -3, -4.

b. McDonnell Douglas

The contract did not limit overtime. Additionally, it was not necessary for the contracting officer to approve overtime before McDonnell Douglas could incur the expense. We find that $11,605,000 challenged

by the Government here is properly awardable to McDonnell Douglas.

4. General Dynamics Offload

General Dynamics transferred a number of tasks to McDonnell Douglas for completion during the course of performance. The audit team grew concerned about costs related to such tasks. "Because the potential duplication of effort has not been quantified by either MDC or GD, Coopers determined that costs associated with this effort may represent costs that GD experienced as overruns." According to defendant, this establishes that plaintiffs did not meet their burden of proving entitlement to these costs: "Neither plaintiff presented evidence as to whether the work in question was a duplication of effort which might be unreasonable for the plaintiffs to recover from the Government."

Mr. Hancock's explanation of the transfer of certain tasks was simple: "McDonnell Douglas could build them quicker than General Dynamics could." He testified that he knew of no duplication of function, even though "[t]owards the latter part of 1990, the issue was discussed at almost every meeting."

We have no basis to suspect duplication of efforts between plaintiffs other than, as Miller termed it during trial, "healthy auditor skepticism." We found no evidence of duplication. This cost is properly awardable.

5. Relocation Expenses

a. General Dynamics

The Government challenges relocation costs of $2,931,977 incurred by General Dynamics. Defen-

dant states that the "benefitting" contract should be charged for the relocation expenses and not the A-12 contract. That is, "if an employee is transferred to another program, for example, the F-16 or the F-18, then those programs and not the A-12 should pay for those costs." Defendant invokes *FAR* 31.205-35(e), which provides that "costs of family movements and of personnel movements of a special or mass nature are allowable. The costs, however, should be on the basis of work (contracts) or time period benefited."

General Dynamics argues that these relocation expenses benefitted the A-12 contract within the meaning of FAR 31.205-35(e). Further, the costs are properly allocable to the A-12 contract as continuing costs after termination, pursuant to *FAR* 31.20542(b). To perform the contract, General Dynamics relocated employees from Ft. Worth to assignments in other locations, such as St. Louis, Tulsa, Patuxent River, and Alamogordo. These employees returned to Ft. Worth after termination. General Dynamics included the costs of returning such employees to Ft. Worth in its Best and Final Offer, which makes these expenses an "explicit premise of the contract."

FAR 31.205-42(b) provides that "costs which cannot be discontinued immediately after the effective date of termination are generally allowable." The DCAM provides, in illustrating this FAR provision:

> For example, the contractor may have contract personnel at a remote or foreign location or there may be personnel in transit to or from these sites. The cost of

> their salaries or wages would be allocable to the terminated contract for a reasonable period required to transfer the personnel to sites for termination or used on the contractor's other work.

DCAM 12-305.7(a)(1).

"No principled distinction can be drawn between the cost to relocate an employee after termination and the cost of that employee's salary while he relocates," according to General Dynamics. We agree, especially because the BAFO included a reference to relocation. The costs incurred to return the contractors' employees to their home base after termination are allocable to the A-12 contract. They are properly included in plaintiffs' termination for convenience recovery.

b. McDonnell Douglas

The Government challenges $78,000 in relocation costs claimed by McDonnell Douglas. Relocation costs were included in the contractors' proposals. As stated above, *FAR* 31.205-42(b) recognizes that "costs which cannot be discontinued immediately after the effective date of termination are generally allowable." The DCAM provision illustrating *FAR* 31.205-42(b) provides examples of allowable termination costs, but they are not meant to be exhaustive. When a contract is terminated, the DCAM contemplates that the salary or wages of a worker may be charged to the terminated contract for a reasonable period, while he is transferred to perform other work or for termination activities. The cost of relocating McDonnell Douglas' employees is similar to the example

provided by the DCAM. McDonnell Douglas' relocation costs are properly awarded.

6. Application of Overhead Rates to Unallowable Costs

The Government notes that "to the extent that unallowable cost is identified, a corresponding adjustment to the amount of overhead costs needs to be made. In essence, if the direct costs are reduced then overhead costs must also be reduced by the approved rate to reflect the proper amount of overhead cost." We agree. The adjustment stemming from our sustaining the Sierra Alloys challenge is $80,144. The deduction in overhead costs resulting from the Government's Stewart-Warner challenge is $86,511. Thus, an additional $166,655 will be deducted from plaintiffs' incurred cost total.

7. Miscellaneous Costs

a. McDonnell Douglas Helicopter Corporation Purchases

During audit field work at the McDonnell Douglas Helicopter Corporation (MDHC), Coopers identified $785,370 in inventory which was common to other programs and which MDC was attempting to charge to the A-12 in violation of *FAR* 31.205-42. MDHC was unable to provide documentation to support the incurrence of $166,000 of direct material costs. There was also $84,865 in costs based on the use of billing rates rather than proposed rates. Finally, Coopers questioned $41,441 for incorrectly applied material handling charges. The total amount of costs challenged relating to MDHC is $1,077,976.

We are generally satisfied with the measures taken by plaintiffs in dealing with common inventory. An earlier discussion describes the testimony that we heard from Mr. Miller and Mr. Hancock relating to common inventory. While the common inventory portion of this challenge is not a concern, we are not satisfied that McDonnell Douglas has proven its entitlement to the other costs challenged by the Government. The Government's challenge is sustained in the amount of $292,306.

b. Douglas Aircraft Company Purchases and Common Bomb Racks

Coopers identified and questioned $1,087,141 in direct material cost for which Douglas Aircraft Company could not provide proper accounting documentation to support the purchase. The costs incurred were for bomb racks that were built initially for the A-12 at Douglas Aircraft Company. Prior to termination, the task of building the racks was transferred to McDonnell Douglas Helicopter Corporation. Separately, Coopers challenged $224,516 in costs incurred by Douglas Aircraft Company related to common bomb rack materials. Mr. Miller testified that the audit team was not provided with adequate documentation as to the propriety of these costs.

Mr. Cromer offered testimony supporting these costs. While documentation of the costs may not have been ideal, the costs were documented nevertheless. Two sets of data were provided; they more or less supported each other. The first was McDonnell Douglas' cost analysis reports reflecting amounts billed by Douglas Aircraft Company. The second consisted of

Douglas Aircraft's cost incurrence records, including requisition forms and "purchase order activity forms."

These costs may not be documented sufficiently to satisfy the rigorous accounting standards employed by Mr. Miller. We find, however, that these costs are reasonable, allowable, and allocable.

c. Loss on Sale of Office Furniture

Mr. Miller questioned the cost of office furniture as common items because such costs are expressly disallowed by *FAR* 31.205-42. In its termination for convenience proposal, McDonnell Douglas claimed a $1,262,000 loss on the sale of Tulsa facility furniture. Mr. Hancock testified that except for a limited amount of furniture that was transferred for the Government's credit, the furniture was in excess of McDonnell Douglas' needs, and could not be used elsewhere after termination despite efforts by McDonnell Douglas to find an alternative use.

Testimony at trial established that the furniture was purchased for the A-12 contract, and that it was sold at auction after termination. McDonnell Douglas claims the resulting loss. The costs appear to have been reasonable, allocable, and allowable. *See generally FAR* 31.205-16(a) (gains and losses from the sale, retirement, or other disposition of depreciable property shall be included in the year in which they occur).

d. Termination Training

Coopers & Lybrand challenges $198,000 for termination training provided by Petersen & Co. be-

cause it was not specific to the A-12 program. Mr. Hancock's testimony, however, established that this training was provided because the A-12 contract was terminated, and was not attended by non-A-12 personnel. We cannot conclude that these costs were not reasonable, allocable and allowable. These costs are properly considered settlement expenses under FAR 31.205-42(g).

e. Non-Standard Overhead Rate

Coopers & Lybrand disallowed $29,000 because McDonnell Douglas used "an incorrect rate for non-standard overhead applied to termination labor." Mr. Miller testified that the use of that rate was not in compliance with the Cost Accounting Standards (CAS) incorporated by FAR Part 31.

Mr. Cromer testified that the $29,000 figure "represents the difference between the nonstandard forecasted rate being applied at September '93 when the initial claim was prepared, versus the year-end rate that was ultimately booked into the accounting records." The correct rate was substituted for the non-standard overhead rate in the 1997 update when the correct rates became available. We do not question Mr. Cromer's credibility on this point. [16]

[16] Additional testimony provided as follows:

Q: When the 1994 update was prepared, it used September 1993 data?

A: That is correct.

Q: And as of September 1993, were there final nonstandard overhead rates for the year 1993?

A: No, there was not.

f. Robotic Paint and Assembly Pump

Coopers questioned $2,978,763 in costs related to a robotic paint and assembly pump. Mr. Miller testified that during the audit inquiry, McDonnell Douglas told the audit team that costs associated with this robotic paint and assembly pump were to be removed from the termination proposal because another program could use it. Instead of removing these costs from its claim, however, McDonnell Douglas increased the costs claimed for this equipment. The Government challenges these costs as being related to common items that are disallowed under *FAR* 31.205-42(a). Miller's challenge is "based solely on his erroneous belief that the sprayer could be used on another program," according to McDonnell Douglas. Mr. Hancock testified that McDonnell Douglas tried to find a use for the sprayer elsewhere-for a while, it appeared that the sprayer could be used in the F/A-18 program-but ultimately no need for the sprayer arose. This testimony was undisputed.

Q: Are there currently rates for 1993 like that?

A: Yes, there are.

Q: Final rates?

A: Yes.

Q: Are there also final rates for 1994, '95 and '96?

A: Yes, there are.

Q: Are those final rates used in the 1997 update?

A: The final nonstandard overhead rate is used for all of those years, yes.

The costs associated with the robotic paint sprayer are allowable, allocable and reasonable. Costs of idle facilities are allowable if they are necessary when acquired and are idled because of changes in requirements that could not reasonably have been foreseen. *See FAR* 31.205-17.

8. Miscellaneous Costs

a. Computer Sciences Corporation-Depreciation Charges

Coopers & Lybrand challenged $54,879 "related to depreciation expenses of computer equipment." The audit team sought documentation from General Dynamics supporting these costs, but these efforts were unsuccessful, according to the Government.

General Dynamics responds that "the total amount of CSC depreciation was over $4 million, all but $54,879 of which had been reconciled." General Dynamics contends that it could have easily spent more than $54,000 trying to resolve the remaining $54,000. This would have resulted in potential Government liability not only for the $54,879 in depreciation, but also for the cost of the reconciliation effort. Settlement expenses might include "[a]ccounting, legal, clerical, and similar costs reasonably necessary for ... [t]he preparation and presentation, including supporting data, of settlement claims to the contracting officer." *FAR* 31.205-42(g)(1)(i), (i)(A). Because the Government did not assist with close-out of this contract, General Dynamics had to determine on its own the proper level

of expenditure to undertake to substantiate its claims. *See generally FAR* 49.201(c).[17]

The Government challenges only a small amount of CSC depreciation expense. Virtually all of the depreciation was properly reconciled (almost 99%), and we agree with plaintiff that chasing the remaining few dollars would not have been in the Government's interest. The total amount claimed is allowable, allocable, and reasonable.

b. Retention Bonuses

Coopers challenged $1,196,000 related to retention bonuses because it said that General Dynamics did not have a "preestablished policy" for giving such bonuses. Mr. Miller testified that retention bonuses were paid by General Dynamics to non-General Dynamics employees.

FAR 31.205-6(a) provides, inter alia:

> Compensation for personal services is allowable subject to the following general criteria and additional requirements contained in other parts of this cost principle:
>
> ....
>
> (3) The compensation must be based upon and conform to the terms and conditions of the contractor's established compensation plan or practice followed so consistently as to imply, in effect, an agreement to make the payment.

[17] *See supra* note 1.

The Government relies on the wrong FAR provisions, according to General Dynamics. It had to retain certain key employees to assist in contract closeout, to maintain program security, and to assist with subcontractor settlements. The retention bonuses for such purposes are awardable under FAR 31.205-42(g)(1)(i)-(iii), governing post-termination settlement expenses. This section provides that such settlement expenses are allowable, such as

> (i) Accounting, legal, clerical, and similar costs reasonably necessary for-
>
> (A) The preparation and presentation, including supporting data, of settlement claims to the contracting officer; and
>
> (B) The termination and settlement of subcontracts.
>
> (ii) Reasonable costs for the storage, transportation, protection, and disposition of property acquired or produced for the contract.

See also FAR 52.249-2(f)(3).

FAR 31.205-6(a) applies by its terms only to payments made for services rendered during the period of contract performance, General Dynamics argues. The provision applies only to employees, rendering it inapplicable to those former General Dynamics employees to whom the company paid retention bonuses. General Dynamics argues that even if *FAR* 31.205-6 did apply, the applicable subsection would be *FAR* 31.205-6(f)(1). This subsection requires an established policy just as 31.205-6(f)(1) does, but

General Dynamics maintains that it set up such an established policy before paying any of the bonuses.

General Dynamics' argument is persuasive. *FAR* 31.205-42(g)(1)(i)-(iii) appear to contemplate the situation at hand. The Government benefitted from General Dynamics' retention of key employees, at least indirectly. For example, Mr. Broesche negotiated effectively with subcontractors, resulting in settlements for about half the amount sought by the subcontractors. Although General Dynamics's argument that it had an "established" policy of paying such bonuses is somewhat tenuous, the decision to retain key employees served the best interests of the Government as well as those of General Dynamics. We do not question that judgment.

c. Loss of Useful Value-Material Transfer Credit

The audit team tested a small sample of "transactions involving the transfer of A-12 equipment to the F-16 program" for General Dynamics' "loss of useful value claim." The auditors noted that General Dynamics transferred A-12 equipment to the F-16 program at less than net book value. Net book value at the time was $35,859. The A-12 program was credited only $7,100. The audit team had concerns about and questioned "the difference between the net book value of the item transferred and the credit given to the A-12 program consistent with CAS 409 [Capitalization of Equipment]." The Government challenges $28,759 in costs.

General Dynamics responds that "the $28,759 in equipment was not A-12 equipment, but was com-

pany-wide equipment charged to an indirect cost pool." It therefore "would have been improper to credit the A-12 contract with costs associated with its transfer because the value of the equipment (unlike the value of the $7,068.82 in equipment that was credited to [the] government) had never been charged to the A-12 contract, as Miller erroneously assumed."

The record before us does not dispute General Dynamics' claim in this regard.

d. Certification Costs

General Dynamics charged the Government $13,000 in certification costs for its updated termination for "convenience proposal," even though this proposal was not certified, according to defendant. Coopers and Lybrand questioned the $13,000 claimed by General Dynamics as unreasonable.

General Dynamics argues that these costs are allowable settlement expenses under the FAR. *See, e.g., FAR* 31.205-42(g)(1)(i)(A) (relating to costs necessary for preparing and presenting settlement claims). It "expended these costs as part of a due diligence review of the McDonnell Douglas portion of the termination for convenience proposal." Mr. Wright testified that the claim of which the Government complains was certified both by McDonnell Douglas and General Dynamics after a review of their June 1991 termination for convenience claim. We do not question these costs.

c. Unsettled Subcontractor Progress Payments

Coopers & Lybrand determined that $1,653,406 in costs "representing unliquidated progress payments made to unsettled subcontractors" is still pending. "The ultimate settlement of these remaining subcontractor claims could result in the repayments of some or all of the outstanding unliquidated amount to General Dynamics," according to the Government.

This challenge deals entirely with unliquidated progress payments made to Harris Corporation. Mr. Wright, who was involved in settlement negotiations with Harris at the time of trial, testified that Harris is entitled to retain at least the $1,653,406 amount, and perhaps more. This amount is not contingent or speculative, therefore, and it is properly awarded to General Dynamics. Wright's testimony is undisputed. This amount is awarded to General Dynamics.

IV. YET TO BE INCURRED COSTS[18]

[18] Defendant notes in its post-trial brief:

> The Government challenges plaintiffs' claim for approximately $26 million in contingent costs not yet incurred. These contingent costs are primarily for program security costs, settlement expenses, and settlement with remaining subcontractors. These costs are unallowable. "Pursuant to *FAR* 52.249-2. Termination for Convenience of the Government (Fixed-Price) the contractor may recover costs incurred in the performance of the work." *Sterling Millwrights, Inc. v. United States*, 26 Cl. Ct. 49, 112 (1992) (emphasis added). Moreover, cost principles expressly prohibit, in FAR

We ruled last year that plaintiffs are entitled to reimbursement of costs that must be incurred in the interest of national security. The "To-Go" portion of costs claimed by General Dynamics for program security through June 1999 is estimated to be $2,489,915. McDonnell Douglas' estimate is $1,910,416. These costs are awarded pursuant to the earlier ruling. McDonnell Douglas has reached a settlement with SCI since the time of trial.[19] Thus, $5 million is no longer a cost yet to be incurred.

McDonnell Douglas' obligation to pay General Dynamics $3.2 million for its efforts in building a turntable is not contingent, and it is therefore included in the judgment. McDonnell Douglas' claim for $2,367,175 for administrative / settlement expenses is denied. Neither the $10,153,895 claimed by General Dynamics for four unsettled subcontractors nor $246,072 claimed for settlement expenses is allowable. We sustain defendant's challenge in the amount of $12,767,142.

CONCLUSION

Plaintiffs claim a total of $3,992,455,272 in reasonable, allocable, and allowable costs. We established a cap on plaintiffs' recovery of $3,499,793,515 for the FSED portion of the contract. Adjusted for funds obligated through the IPR and EPA clauses, the funding cap becomes $3,635,767,376. Adding the

Part 31, recovery of non-incurred, contingent costs. *See FAR* 31.205-7(a) and 7(b).

[19] McDonnell Douglas agreed to pay $8 million pursuant to the settlement, but its claim remains $5 million.

undisputed amounts of $.212 billion for Lot I and $.030 billion for Lot II, we arrive at a figure of $3,877,767,376. Taking into account progress payments of $2,677,634,556 held by plaintiffs, the amount due plaintiffs is $1,200,132,820, plus statutory interest on that sum from June 26, 1991 until paid.

The parties asked us to rule on the total amount of plaintiff's reasonable, allowable and allocable incurred costs, irrespective of the cap. The total amount of reasonable, allowable and allocable costs incurred by plaintiffs is $3,978,002,676. The judgment that we enter today, however, is $1,200,132,820.

The opinion and order of February 20, 1998 is VACATED. The clerk is directed to VACATE the judgment entered February 23, 1998 as well, and to enter judgment for plaintiffs in the amount of $1,200,132,820, plus statutory interest from June 26, 1991 until paid. No costs.

APPENDIX G

United States Court of Federal Claims

McDONNELL DOUGLAS CORPORATION
and General Dynamics Corporation,
Plaintiffs,

v.

UNITED STATES of America,
Defendant.

No. 911204C

Dec. 13, 1996.

OPINION AND ORDER

HODGES, Judge.

In 1988 plaintiffs McDonnell Douglas and General Dynamics contracted with the Navy to develop the A-12, a carrier-based attack aircraft, to replace the Navy's aging A-6. During the course of performance, the contractors experienced numerous problems, particularly with confining aircraft weight growth to the range specified under the A-12 full scale engineering and development contract. By late 1990, they were behind schedule and costs exceeded their estimates. The contractors requested equitable adjustments totaling $1.401 billion to compensate for impossibility of performance and the Government's failure to disclose superior knowledge. The contracting officer terminated the contract for default on January 7, 1991.

We determined after trial that the Government acted improperly, and we vacated the termination for default. In December 1995 we converted the termination for default to a termination for convenience of the Government. *McDonnell Douglas Corp. v. United States*, 35 Fed. Cl. 358 (1996).

Plaintiffs point out that the Federal Acquisition Regulation entitles them to incurred costs plus a reasonable profit in such circumstances. Defendant argues that the FAR requires us to adjust plaintiffs' cost reimbursement amount downward to reflect the loss that they would have sustained had the contract been completed.

The parties seek a trial on damages to resolve plaintiffs' entitlement to profits and defendant's imposition of a loss ratio. Their allegations about the propriety of plaintiffs' superior knowledge claim, and the competing entitlements to profits or a loss adjustment, can be addressed only if both parties are permitted to use information that we have been warned would provoke a formal invocation of the military and state secrets privilege, or cause grave harm to our nation's security interests.[1]

Important information about plaintiffs' claim necessarily will be withheld from plaintiffs' and defendant's litigation teams. Our understanding of

[1] The Executive Branch invoked the military and state secrets privilege to remove from this case some evidence related to superior knowledge issues. Separately, General Merrill A. McPeak filed a declaration warning us about unacceptable risks posed by further discovery and litigation concerning superior knowledge.

this information is sufficient to know that it is necessary to a fair adjudication of plaintiffs' claims or government defenses in certain areas.

We cannot permit the parties to litigate plaintiffs' equitable adjustment claims for three reasons: (1) One party or the other would be unfairly prejudiced due to limitations placed on discovery by the Executive for national security reasons; (2) Highly classified information may be compromised in discovery despite procedures in place to prevent that from happening; and (3) Even if information available to the parties could be protected properly in discovery, other information necessary for the court to render an honest judgment would not be available.

For these reasons, issues involving equitable adjustments, superior knowledge, profits, and loss adjustment will not be litigated further in this court. Plaintiffs may recover their incurred and allowable costs plus interest. Defendant may not obtain a loss adjustment pursuant to *FAR* 49.203, and plaintiffs may not obtain profits pursuant to *FAR* 49.202. This opinion and a classified appendix to be filed separately with the Federal Circuit address the reasons for this ruling.[2]

[2] The Executive has been candid and forthcoming in providing materials for the classified appendix. The appendix necessarily compiles disparate but highly sensitive information in one place. It may not be necessary for anyone to review these materials to resolve the legal issues raised by the parties in this lawsuit. The materials would be relevant only for the purpose of reviewing the trial court's decision to remove these matters from the case without the benefit of formal invocations of appropriate privileges in each instance.

I. TERMINATION FOR CONVENIENCE DAMAGES

When the Government terminates a contract for default, the contractor may not recover its costs for undelivered work, and may have to forfeit any advance or progress payments attributable to that work. *FAR* 49.402-2. When the Government terminates a contract for its convenience, the contractor "should be compensated fairly for the work done and the preparations made for the terminated portions of the contract, including a reasonable amount for profit." *FAR* 49.201. Typically, the contractor is entitled to recover all its incurred costs and settlement costs, and reasonable profits if warranted. *FAR* 52.249-2(f). If it appears that the contractor would have suffered a loss on the entire contract, however, the contractor will not obtain a profit, and its cost recovery will be reduced corresponding to the rate of loss. *Id.*

When deciding the proper amount of a termination for convenience cost recovery, "[t]he contractor has the burden of establishing, by proof satisfactory to the TCO, the amount proposed." *FAR* 49.109-7(c). The contractor's proof is submitted in the form of a settlement proposal. *FAR* 52.249-2(d); FAR 49.104(h). If the Terminating Contracting Officer and the contractor cannot reach a settlement, the TCO must make the determination. *FAR* 49.103(b); 49.109-7. He must do so, however, in compliance with FAR 49.109-1 through 49.109-6, which govern termination for convenience settlement agreements generally, and *FAR* 49.203, which requires that the

cost recovery be adjusted for any loss. *See also FAR* 52.249-2(f).

A. Loss Ratio

The Terminating Contracting Officer decides whether to allow a profit or to adjust the recovery for a loss. *FAR* 49.109-7(a).[3] A loss adjustment reduces a contractor's termination for convenience recovery if the contractor would have sustained a loss on the entire contract. The Terminating Contracting Officer multiplies the incurred costs allowable under the termination for convenience settlement guidelines by a so-called "loss ratio."

Loss Ration = (Original Contract Price + Equitable Adjustments) Estimate at Completion

> *FAR* 49.203(b)(3). Thus, when the Terminating Contracting Officer applies a loss ratio, the contractor receives only a percentage of its allowable costs incurred. A loss ratio begins with an assumption of no profit, and it forces the contractor to bear out-of-pocket costs that otherwise would be paid by the Government.[4] In

[3] In a companion opinion discussing plaintiffs' post-complaint claims, we show why the court has assumed the role of the Terminating Contracting Officer at this stage of the proceeding. *See McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 285 (1997).

[4] *FAR* 52.249-2 Termination for Convenience of the Government (Fixed Price) (APR 1984) provides a framework for determining profit or loss when the contractor and the contracting officer cannot reach a settlement:

short, the adjustment always prevents a contractor from receiving credit for all of its allowable costs-funds that it rightfully spent to perform the contract.

The boards have found that "the Government generally has the burden of proving entitlement to a loss adjustment, including the estimate to complete

> (f) If the Contractor and Contracting Officer fail to agree on the whole amount to be paid because of the termination of work, the Contracting Officer shall pay the Contractor the amounts determined by the Contracting Officer as follows ...:
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> (1) The contract price for completed supplies or services accepted by the Government ... not previously paid for, adjusted for any saving of freight and other charges.
>
> (2) The total of
>
> (i) The costs incurred in the performance of the work terminated, including initial costs and preparatory expense allocable thereto, but excluding any costs attributable to supplies or services paid or to be paid under subparagraph (f)(1) above;
>
> (ii) The cost of settling and paying termination settlement proposals under terminated subcontracts that are properly chargeable to the terminated portion of the contract if not included in subdivision (i) above; and
>
> (iii) A sum, as profit on subdivision (i) above, determined by the Contracting Officer under 49.202 of the *Federal Acquisition Regulation*, in effect on the date of this contract, to be fair and reasonable; however, if it appears that the Contractor would have sustained a loss on the entire contract had it been completed, the Contracting Officer shall allow no profit under this subdivision (iii) and shall reduce the settlement to reflect the indicated rate of loss.

as a necessary ingredient thereof...." *Specon Inc., ASBCA* 29137, 863 *BCA* ¶ 19,163 at 96,855 n.*, 1986 WL 221146; *see also Wolfe Constr. Co., ENGBCA* 5309, 883 *BCA* ¶ 21,122 at 106,655, 1988 WL 100976; John Cibinic, Jr. & Ralph C. Nash, Jr., Administration of Government Contracts 1129 (3d ed. 1994). The fact that a contract appears to be in a loss position at the time of termination does not necessarily mean that a loss adjustment applies. "It is not appropriate to apply the loss adjustment factor or to limit the settlement to the contract price without giving consideration to unpriced changes or other modifications.... However, in some cases the boards will merely ignore the loss adjustment if the contractor is entitled to price adjustments." *Wolfe Constr. Co., ENGBCA* 5309, 883 *BCA* ¶ 21,122 at 106,655 (finding no loss adjustment when Government maladministration warranted upward adjustment in contract price); *see also Astro Dynamics, Inc., ASBCA* 41825, 912 *BCA* ¶ 23,807 at 119,209, 1991 WL 38292 (constructive changes by Government to the contract allows plaintiff to recover costs not required under contract and eliminates imposition of loss adjustment); *M.E. Brown, ASBCA* 40043, 911 *BCA* ¶ 23,293 at 116,816, 1990 WL 158914 (same); *R.H.J. Corp., ASBCA* 12404, 691 *BCA* ¶ 7587 at 35,227, 1969 WL 584 (Government failure to make progress payments contributed to cost enhancement, so no basis for loss); Cibinic & Nash, Administration of Government Contracts 1129 (3d ed. 1994).

It is defendant's burden to prove that plaintiffs would have sustained a loss on the entire contract. When the A-12 contract was terminated, plaintiffs'

costs had overrun the Government's payment schedule, and much work remained before the aircraft would have been operational. Plaintiffs were in financial distress, the Government argues. Had the contract not been terminated, they would have borne even greater losses. Defendant claims that *FAR* 49.203 compels plaintiffs to bear these losses.

Plaintiffs' superior knowledge claim alleges that the Government possessed but did not share with the contractors information about low-observable (Stealth) technology. According to plaintiffs, this information included weight estimation techniques, application of low-observable technologies, propulsion system technologies, composite materials and composite manufacturing technologies, and avionics technologies. Timely knowledge about this information, plaintiffs argue, would have enabled them to solve technical problems without conducting extensive, often duplicative efforts at great expense.

If plaintiffs were permitted to prove their superior knowledge claim, defendant likely could not establish the application of a loss ratio. *See Riverport Industries, Inc., ASBCA* 30888, 87-2 *BCA* ¶ 19,876 at 100,522-24, 1987 WL 40948 (contract price increased after plaintiff proved its superior knowledge claim, constituting a constructive change to the contract). Thus, one of plaintiffs' defenses to a loss ratio depends on whether they can prove their superior knowledge allegations.

B. Profits

The Terminating Contracting Officer awards profits to the contractor "on preparations made and

work done by the contractor for the terminated portion of the contract but not on the settlement expenses." *FAR* 49.202(a). The Terminating Contracting Officer may not award anticipatory or consequential profits. *Id.*; *G.L. Christian & Assoc. v. United States*, 160 Ct. Cl. 1, 11, 15-17, 312 F.2d 418, 423, 426-27, *cert. denied*, 375 U.S. 954, 84 S. Ct. 444, 11 L. Ed. 2d 314 (1963); *General Builders Supply Co. v. United States*, 187 Ct. Cl. 477, 485, 409 F.2d 246, 251 (1969). The TCO must "arrive at a fair profit" by any reasonable method. *FAR* 49.202(a). No monolithic formula for determining profits is available; the FAR provides an extensive list of discretionary factors for the Terminating Contracting Officer to consider.[5] "Determination of the rate of profit is done

[5] FAR 49.202(b) and (c) provide:

> (b) In negotiating or determining profit, factors to be considered include-
>
> (1) Extent and difficulty of the work done by the contract as compared with the total work required by the contract (engineering estimates of the percentage of completion ordinarily should not be required, but if available should be considered);
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> (2) Engineering work, production scheduling, planning, technical study and supervision, and other necessary services;
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> (3) Efficiency of the contractor, with particular regard to-
>
> (i) Attainment of quantity and quality of production;
>
> (ii) Reduction of costs;
>
> (iii) Economic use of materials, facilities, and manpower; and

on a case-by-case basis and the application of the regulatory guidelines is considered a matter of judgment." Cibinic & Nash, Administration of Government Contracts 1128 (3d ed. 1994) (citing *Metered Laundry Servs., ASBCA* 21573, 78-1 *BCA* ¶ 13,206, 1978 WL 2351, *modified on recons.*, 78-2 *BCA* ¶

(iv) Disposition of termination inventory;

(4) Amount and source of capital and extent of risk assumed;

(5) Inventive and developmental contributions, and cooperation with the Government and other contractors in supplying technical assistance;

(6) Character of the business, including the source and nature of materials and the complexity of manufacturing techniques;

(7) The rate of profit that the contractor would have earned had the contract been completed;

(8) The rate of profit both parties contemplated at the time the contract was negotiated; and

(9) Character and difficulty of subcontracting, including selection, placement, and management of subcontracts, and effort in negotiating settlements of terminated subcontracts.

(c) When computing profit on the terminated portion of a construction contract, the contracting officer shall

(1) Comply with paragraphs (a) and (b) above;

(2) Allow profit on the prime contractor's settlements with construction subcontractors for actual work in place at the job site; and

(3) Exclude profit on the prime contractor's settlements with construction subcontractors for materials on hand and for preparations made to complete the work.

13,451, 1978 WL 2366). Whether to award profit in this case is a matter of discretion for the court.

Plaintiffs argue that once they have proven their superior knowledge-based claim, corresponding equitable adjustments would increase the price of the A-12 contract enough to avoid the imposition of a loss ratio and entitle them to profits. Plaintiffs seek an opportunity to prove their equitable adjustment claims.

Defendant maintains that additional discovery and trial would not support plaintiffs' argument that the Government withheld critical information during performance. The present state of superior knowledge discovery does not verify plaintiffs' allegations, according to defendant. Even if it did, further inquiry into various "black" programs would undermine plaintiffs' argument.

II. SUPERIOR KNOWLEDGE

The A-12 was designed to employ low-observable technology to elude enemy radar and defense systems. This technology is highly classified and it remains vital to our nation's security. When the A-12 contract was executed, the Air Force already had conducted flight tests for the B-2 Bomber and the F-117A Fighter through participation with other contractors. Low-observable technology had been applied and tested by 1988, at least according to B-2 and F-117A specifications. The A-12 was designed to apply similar technology.

Plaintiffs were anxious to access B-2 and F-117A program information during contract performance, and they had reason to expect that they would be

granted such access.[6] Ultimately they were given access to these programs, but access came too late according to plaintiffs.

Plaintiffs' superior knowledge claim alleges that the Government possessed information that it was required to share for the benefit of contract performance.[7] Through trial and error the Government had

[6] The Government contemplated sharing information with the contractors. "To take advantage of previous technologies developed by the USAF and minimize life cycle costs, the Navy and the Air Force were directed to form a joint committee to minimize duplication of development efforts on the [A-12] and the USAF Advanced Tactical Fighter (ATF)." ATA Acquisition Strategy, NAVAIR Doc. 201//0182-86, 7/12/86, para. I.C. Other evidence supports this assertion as well. During his deposition, Secretary of the Navy John Lehman remarked:

> there was an unquestioned assumption when we started the [A-12] program that [the Navy] would have full and unimpeded access to all of the B-2 technology.
>
> ....
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> ... since the airplane was to be a miniature B-2, which would face all of the same unstable flight control issues, all of the same wind tunnel expenses, all of the same issues of dealing with engine inlets and outlets, it was just a smaller version of the B-2, that an enormous amount of money could be saved in wind tunnel time and development process by simply using the Air Force Northrop data.

Lehman Dep., at 104-05 (July 26, 1995).

[7] Earlier in this litigation, the Government argued that it had no duty to provide such information because the contract did not require it to share classified superior knowledge. We ruled that plaintiffs alleged an actionable claim. *McDonnell Douglas Corp. v. United States*, 27 Fed. Cl. 204, 206 (1992) (ruling that defendant has a duty under *J.A. Jones Construction Co. v.*

learned that certain approaches to the design and development of the B-2 and F-117A were preferable to others, according to plaintiffs. Lacking this background, plaintiffs complain that A-12 performance specifications were impossible to accomplish within the time and cost projections contemplated by the parties.

Defendant argues that plaintiffs' claim is groundless because their participation in other highly classified Air Force programs informed them about methods necessary to develop the A-12 according to specifications. The Government argues that if we would permit such evidence, defendant could demonstrate that plaintiffs possessed information and experience that negate a credible superior knowledge claim.

We terminated discovery in August 1993 because the Executive warned us that discovery could not be conducted safely. *See McDonnell Douglas Corp. v. United States*, No. 91-1204 (Fed. Cl. Aug. 11, 1993). Limited discovery resumed in April 1994 after plaintiffs persuaded us that accessible information could be segregated from non-accessible information. In April 1995 the court became aware that new problems would arise. We no longer believed that plaintiffs could segregate information safely, and closed discovery.

United States, 390 F.2d 886 (1968) to provide plaintiffs at least a "general warning" about problems concerning production of the aircraft).

A. Security Procedures

Portions of the B-2 and F-117A are in Special Access programs. Generally, there are three levels of classification: Top Secret, Secret, and Confidential. Agency heads are authorized to label programs Special Access when safeguards applicable to Top Secret and Secret are not sufficient to protect them. Access to such programs can be achieved only through special procedures. Admission is governed strictly by a controlling agency and granted sparingly on a "need-to-know" basis.[8] Only those essential to the program who meet all stipulated security requirements may view Special Access program information.

We established strict security measures to protect classified information in this case. Professional security officers who are trained to safeguard sensitive information have helped the court manage discovery. We have been assisted by agency personnel who control access to classified and Special Access programs. Officials from the Department of Defense advised the court about the nature and the importance of information at stake through classified and unclassified declarations and briefings. We fashioned protective orders to accommodate these concerns while preserving the adversary process to the extent possible. Still, problems have occurred.

[8] Oddly, this important term is defined differently by various controlling agencies.

B. Security Problems

1.

During an informal conference that we conducted periodically to facilitate discovery, counsel for General Dynamics informed the court that a request for access to certain information had been pending with the Government for an inordinate period of time. We asked government counsel to look into the matter and have the appropriate person make a decision. Counsel for General Dynamics also informed the court that his request for access was in the custody of the Navy's Litigation Team. This was troubling because we had ordered that security matters and litigation matters be kept strictly separate.

We determined that General Dynamics had made the request so that an employee of the company could communicate certain information to its counsel. Government counsel was unwilling or unable to tell the court why access for the attorney had been denied, and we instructed the Government to provide someone who could explain. The Government arranged a meeting for the court with Air Force Colonel John B. Hennessey, who described the nature of the request and his reason for declining it to plaintiffs' counsel. He assured the court that the Government's litigation team knew nothing about the information either. This was true so far as the Air Force knew, but it turned out that the information had been given to government lawyers by the Navy.[9]

[9] A number of government attorneys and management personnel gained access to this Air Force information improperly through the Navy. The Navy did not have authority to brief the

We ruled that the Government could not give its own lawyers access to information for litigation purposes that at the same time it was prohibiting General Dynamics from giving to its lawyers.

In March 1993, Acting Secretary of the Air Force Michael B. Donley invoked the military and state secrets privilege to protect the information at issue.[10] Court security officers briefed the court *in camera* about this information and other information outside A-12 parameters that warranted our attention. We reviewed the information over which the privilege was asserted very carefully in an effort to isolate non-sensitive information. This review led to recommendations concerning means of advising plaintiffs' counsel of certain general concepts. Our concern was

Government's litigation team about the Air Force information. Plaintiffs' attorneys were not permitted to communicate with their client about information that defendant's attorneys not only had discussed with theirs, but also used in developing their defense to superior knowledge claims. This knowledge contributed to a serious security breach later.

[10] We asked the Government to explain why its litigation team was given information so sensitive that the Air Force Secretary declared its disclosure for purposes of this litigation to be a threat to national security. The Government represented to the court that its lawyers needed access to the information so that they could defend the military and state secrets privilege. In fact, government lawyers obtained access to Air Force secrets long before the matter came to the attention of the Secretary of the Air Force. *See McDonnell Douglas Corp. v. United States*, No. 91-1204 (Fed. Cl. Dec. 23, 1993). We issued sanctions against the United States for this and related misrepresentations, and later removed them at the request of the Assistant Attorney General who stated that he would take corrective action.

that plaintiffs' counsel might ask questions or make arguments that would compromise this information through inadvertence. Security officials were not willing to brief the concepts.

Later, we encouraged the Government to broaden its invocation of the military and state secrets privilege to include additional sensitive information that we expected to encounter. The Air Force expressed its concern for harm to national security if discovery were to proceed on these matters, but it chose not to formally invoke the military and state secrets privilege to protect them.

2.

Plaintiffs' counsel deposed Richard L. Rumpf, a former Navy official who had served as Deputy Assistant Secretary of the Navy, and Acting Assistant Secretary of the Navy. Mr. Rumpf was familiar with A-12 program classification guidelines as well as programs classified outside the A-12 program. He had been instructed to confine his answers to A-12 program information only. As noted earlier, Government counsel defending the deposition had gained access to pertinent information that had been denied plaintiffs' counsel.

Plaintiffs' counsel, not having been briefed prior to the deposition, asked questions to which Mr. Rumpf responded concerning matters outside the A-12 program. Mr. Rumpf conferred with security personnel and answered plaintiffs' questions in the belief that he was authorized to make such disclosures. He was not. Government counsel exacerbated the problem by asking Mr. Rumpf highly inappropriate,

leading follow-up questions designed to elicit responses that would benefit defendant's legal position. This resulted in still more disclosures about information classified outside the A-12 program. No one acted to correct the mistake then, and complete transcripts of the deposition were distributed.

During a March 1993 courtroom hearing, plaintiffs' counsel read excerpts from the tainted deposition into the record. No immediate corrective action was taken. Hearing transcripts were distributed to the parties and used as an unclassified document. Plaintiffs' attorneys and personnel referenced portions of Mr. Rumpf's deposition in their notes and other internal memoranda. Plaintiffs quoted from and cited to the Rumpf deposition in pleadings issued to this court and to the Federal Circuit.

The Government did not identify a breach until mid-April 1993. It took steps to remedy the damage, but a series of miscalculations compounded the problem. The result was that plaintiffs' attorneys were exposed to information that they were not cleared to know.

3.

Plaintiffs deposed Admiral David Jeremiah, Vice Chairman of the Joint Chiefs of Staff, in July 1993. Admiral Jeremiah was familiar with information to which plaintiffs' attorneys had been denied access. Plaintiffs' counsel, still not briefed about concepts that should have been avoided, prompted Admiral Jeremiah into a discussion about information not authorized for disclosure. Defendant's attorney did not intervene. Admiral Jeremiah's comments were tran-

scribed, and several days later security officials were forced to seize transcripts that had been distributed.

III. JUSTICIABILITY

A. Military and State Secrets Privilege

The military and state secrets privilege grants the Executive the exclusive right to bar discovery of certain military secrets. *United States v. Reynolds*, 345 U.S. 1, 73 S. Ct. 528, 97 L. Ed. 727 (1953). That is, discovery into specific, classified areas may be terminated by the declaration of an appropriate official. *Id.* at 78, 73 S. Ct. at 531-32; *Ellsberg v. Mitchell*, 709 F.2d 51, 57 (D.C. Cir. 1983) ("When properly invoked, the state secrets privilege is absolute.").

Invocation of the military and state secrets privilege is proper if the court finds that the appropriate person signed it (head or acting head of the agency that controls the secret), the person did so after careful consideration, and the person used the proper words to invoke the privilege. *Reynolds*, 345 U.S. at 78, 73 S. Ct. at 531-32. Once satisfied of these formalities, the court may review and evaluate the subject material in camera. "The court itself must determine whether the circumstances are appropriate for the claim of privilege, and yet do so without forcing a disclosure of the very thing the privilege is designed to protect." *Id.* at 8, 73 S. Ct. at 532 (footnotes omitted). If the proper official has declared that the risk of disclosing the privileged information is a significant threat to the nation's security, the information must be removed from the case.

1. *Reynolds*

United States v. Reynolds is the source of much state secrets privilege jurisprudence. In that case, three civilian observers aboard an Air Force B-29 were killed when an engine exploded, causing the aircraft to crash. At the time of the accident the Air Force was testing secret electronic equipment aboard the aircraft. Widows of the deceased brought their consolidated actions against the United States pursuant to the Federal Tort Claims Act, 28 U.S.C. §§ 1346, 2674. In pretrial discovery, plaintiffs moved to obtain the Air Force's official accident investigation report and narratives from three surviving crew members.

The Government responded first by moving to quash this request on the grounds that the report and narratives were privileged matters according to Air Force regulations. The trial court disagreed. This prompted the Secretary of the Air Force to write the trial court and explain that the report could not be disclosed because "the aircraft in question, together with the personnel on board, were engaged in a highly secret mission of the Air Force." *Reynolds*, 345 U.S. at 4, 73 S. Ct. at 530.

The court requested *in camera* review of the report to evaluate the validity of the Government's position, but the Government refused. The court assessed Rule 37 sanctions, held a hearing on damages, and entered final judgment for plaintiffs. The case was affirmed on appeal, but the Supreme Court reversed and remanded for further proceedings. It also

set forth the protocol for trial courts to observe when confronted with the state secrets privilege.

Thus, *Reynolds* directs trial courts to oversee proper invocation of the state secrets privilege and to remove evidence from the case when warranted. *Reynolds'* progeny struggle to define the result of that action. With evidence removed from the case, should the court proceed? If not, who wins? What must the plaintiff show to keep its claim alive? Conversely, how may the Government defend itself?

2. *Farnsworth*

A contractor sued a Navy employee for wrongful interference with prospective contractual relations in *Farnsworth Cannon, Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (en banc) (per curiam). Inquiries about Grimes' responsibilities within the Navy led the Secretary of the Navy to invoke the state secrets privilege. The invocation was proper, and Grimes moved to dismiss the case against him. The trial court granted his motion on the basis that the plaintiff was manifestly unable to prove its case without the state secret. The Fourth Circuit affirmed the trial court's decision en banc, citing its concern about the danger of interrogating witnesses in open court about sensitive matters. "In an attempt to make out a prima facie case during an actual trial, the plaintiff and its lawyers would have every incentive to probe as close to the core secrets as the trial judge would permit. Such probing in open court would inevitably be revealing." *Id.*

Had there been enough nonprivileged information available for the plaintiff to make a prima facie case

without jeopardizing privileged information, perhaps the case could have advanced. *Accord Halkin v. Helms*, 690 F.2d 977, 998-99 (D.C. Cir. 1982) (*Halkin II*) (without access to privileged information, plaintiffs could not state claim or prove injury in fact to trigger standing). [11]

3. *Ellsberg*

In *Ellsberg v. Mitchell*, 709 F.2d 51 (D.C. Cir. 1983), former defendants in a criminal action brought suit against government officials responsible for conducting warrantless surveillance activities. They sought specific responses about wiretaps from the Government. This prompted several high-ranking government officials, including the Attorney General, the Director of Central Intelligence, and the Secretary of Defense, to invoke the state secrets privilege to protect against disclosure of information related to numerous "overhears" of plaintiffs' private conversations. The district court reviewed affidavits *in camera* and concluded that disclosure would cause adverse consequences for national security. Defendant then filed a motion to dismiss, and the court entered partial judgment for the Government. On appeal, the district court's decision was reversed and remanded for additional proceedings. Here, the Circuit court thought that enough nonprivileged infor-

[11] At least one court has interpreted Farnsworth to mean that when a plaintiff possesses privileged information, and therefore has an incentive to draw as close as possible to the bounds of disclosure to prove its case, dismissal should automatically follow an invocation of the privilege. *Ellsberg v. Mitchell*, 709 F.2d 51, 65 (D.C. Cir. 1983) (dicta).

mation was available for some of the plaintiffs to assemble a *prima facie* case.

4. *Zuckerbraun*

Defense contractors in *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544 (2nd Cir. 1991) were sued for negligent design, manufacture, testing, and marketing of the antimissile defense system aboard the U.S.S. Stark, a Navy frigate stationed in the Persian Gulf. In 1987, a missile launched from an Iraqi jet fighter escaped the Stark's defenses and killed 37 crewmen. The executor for one member of the crew brought suit. Representatives of 23 other deceased crewmen filed their own actions in a separate suit, which was appealed to the Fifth Circuit in *Bareford v. General Dynamics Corp.*, 973 F.2d 1138 (5th Cir.1992).

The allegations in *Bareford* substantially paralleled those asserted in *Zuckerbraun*. In both cases, defendants moved to dismiss because the subject matter was barred by the military and state secrets privilege. Secretary of the Navy H. Lawrence Garrett, III invoked the privilege properly, and demonstrated the grave risks that would accompany disclosure of the protected information. Both courts ruled that dismissal was proper. In *Bareford*, the plaintiffs provided over 2,500 pages of information to support their case, but the court curtailed proceedings because the plaintiffs alleged defects for which proof-if it existed-was barred by the privilege. Liability depended on whether the defendants were negligent, and "[t]hese questions cannot be resolved or even put in dispute without access to data regarding

the design, manufacture, performance, functional characteristics, and testing of these systems and the rules of engagement under which the Stark was operating." *Zuckerbraun*, 935 F.2d at 547.

5. *Molerio*

Invocation of the state secrets privilege may produce harsh results. The plaintiff may be unable to prove its case; the Government may be unable to defend itself. The latter consequence has led to the dismissal of a case in which a jury would have been led to false conclusions without the secret information. *Molerio v. FBI*, 749 F.2d 815, 825 (D.C. Cir. 1984).

In *Molerio v. Federal Bureau of Investigation*, plaintiff sued the FBI for illegally and unconstitutionally refusing to hire him as a special agent. One of the charges alleged that the FBI's decision was unconstitutional because it was "based at least in part on the political activities and beliefs of his father." *Id.* at 824. The state secrets privilege was properly invoked and included an affidavit describing the FBI's reason for denying employment to plaintiff. The reason was sensitive, and its disclosure would have impaired national security. After in camera review, the court determined that the reason Molerio was not hired "had nothing to do with [his father]'s assertion of First Amendment rights." *Id.* at 825. Having the benefit of information provided in camera, and cognizant of the fact that perhaps enough circumstantial evidence existed on the surface for the plaintiff to lead a jury into factual error, the court terminated proceedings.

Presenting such a case to the jury, even on the basis of nonprivileged information, would have "involve[d] an attempt, however well intentioned, to convince the jury of a falsehood." *Id.* The court declined to entertain a sham proceeding. "Although there may be enough circumstantial evidence to permit a jury to come to [an] erroneous conclusion, it would be a mockery of justice for the court-knowing the erroneousness-to participate in that exercise." *Id.* The D.C. Circuit subsequently interpreted *Molerio* to mean that when privileged material would establish a genuine defense, summary judgment against the plaintiff is proper. *In re United States*, 872 F.2d 472, 476 (D.C. Cir. 1989) (dicta).

B. Unfair Prejudice

Ten representatives from plaintiffs' litigation team have access to B-2 and F-117A program information. The Government's litigation team enjoys similar access. But the B-2 and F-117A are only two programs employing low-observable technology. If other programs are relevant, they will not be used in this case, and one party or the other would be unfairly prejudiced as a result.

Plaintiffs have maintained that they could prove superior knowledge within the confines of the programs to which they have been given access. That may be true. We do not doubt plaintiffs' ability to present a persuasive case based on this information alone. But defendant may be unfairly prejudiced if discovery were restricted to these programs. Secretary Donley's declaration is illustrative. The evidence that he protected by invoking the military and state

secrets privilege was classified beyond A-12 program information.

Defendant has contended that it could demonstrate plaintiffs' expertise in the techniques, design, and composite characteristics necessary to develop the A-12 according to specifications. Just as we acknowledge plaintiffs' belief that they could prove superior knowledge within the confines of the A-12 program, we know that the Government may have defenses based on the factors described in *Helene Curtis Industries, Inc. v. United States*, 160 Ct. Cl. 437, 312 F.2d 774 (1963).[12] Plaintiffs are involved in other programs with the Government; it is possible that they did not lack knowledge about low-observable technology.

Plaintiffs state that whether the Government may defend itself by asserting evidence from other Stealth programs should not concern the court. It does concern us, however, for the same reason that we did not dismiss plaintiffs' claim when Secretary Donley invoked the privilege. We gave plaintiffs an opportunity to make a prima facie showing that they could make a case without the privileged information. A claim should be dismissed if a *prima facie* showing cannot be accomplished safely, or if it would lead to a false result. *See Farnsworth Cannon, Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (en banc)

[12] *Helene Curtis* requires a plaintiff to establish the following elements: (1) defendant possessed the information; (2) plaintiff neither knew nor had reason to know the information; (3) defendant did not supply the information; and (4) plaintiff was therefore misled.

(per curiam); *Molerio v. FBI*, 749 F.2d 815 (D.C. Cir. 1984). To avoid unfair prejudice to defendant, we apply the same principle.

> If the information is essential to establishing plaintiff's prima facie case, dismissal is appropriate.... If, on the other hand, the information related not to plaintiff's claim, but rather to the defense, summary judgment against the plaintiff is proper if the district court decides that the privileged information, if available to the defendant, would establish a valid defense to the claim.

In re United States, 872 F.2d at 476 (citing *Molerio*, 749 F.2d at 825). If we were to try the claim on the basis of plaintiffs' *prima facie* evidence, defendant may be unable to defend itself. Plaintiffs argue that we may try this case on a limited basis. We have searched for ways to do this, but the result could be unfair to one or both parties. A trial would not be conclusive.

At trial, plaintiffs would establish their superior knowledge claim. Defendant would seek to reply by presenting evidence of plaintiffs' exposure to relevant information through involvement with non-A-12 programs. If permitted to present this information, defendant possibly would not be prejudiced. But might other information redeem plaintiffs' allegations in rebuttal? Plaintiffs would not know. This scenario would recur in different forms in the course of discovery or trial. The Executive necessarily would block the parties' probing at some point, and such an

invocation of the military and state secrets privilege would cease discovery or testimony. The timing of the privilege would determine who among the litigants would be damaged. The Executive's job is to protect its secrets; it has no obligation to find the truth.

C. High Risk Information

Unique materials and components whose efficacy has been proven in the B-2 and F-117A programs enable those aircraft to exploit low-observability characteristics. The B-2 and F-117A programs now are acknowledged programs. The public knows that these programs exist, though the materials and component information critical to the effectiveness of low-observable features remains closely guarded. We may not defend easily against an enemy that would acquire such information, so significant risks would accompany discovery of matters related to these components and materials. But such discovery could be conducted with manageable risk. The United States is proficient at protecting technical jargon that explains tangible features of a known product. The Air Force and the Navy have means to suppress or eliminate this risk.

This case involves more than technical, "blueprint" information about the B-2 and F-117A, however. Discovery in this litigation has swept us against less concise yet potentially more vulnerable compartments of knowledge. Inadvertent disclosure of their existence may be tantamount to full disclosure.

When Acting Secretary Donley invoked the military and state secrets privilege, he made the following observation:

> The mere existence of an unacknowledged program is classified within the boundaries of the special access program. That is, one must be approved for access before one may know that the program exists at all.

Donley Decl. at 4. If discovery were allowed to proceed and the Air Force invoked the military and state secrets privilege only as to certain matters, an attentive observer could establish an informed impression of this privileged information.

> [I]f a witness is questioned about facts A and B, the witness testifies that fact A is not a military secret, and the government objects to any answer regarding fact B, by implication one might assume that fact B is a military secret.

Bareford v. General Dynamics Corp., 973 F.2d at 1143 (citing *Fitzgerald v. Penthouse International Ltd.*, 776 F.2d 1236, 1243 n.10 (4th Cir. 1985)).[13]

[13] The *Bareford* court explained that

> in some cases it is appropriate that the courts restrict the parties' access not only to evidence which itself risks the disclosure of a state secret, but also those pieces of evidence or areas of questioning which press so closely upon highly sensitive material that they create a high risk of inadvertent or indirect disclosures.

Bareford, 973 F.2d at 1144.

The classified information in *Reynolds* related to experimental electronics equipment aboard an Air Force B-29. The plaintiffs sought an explanation for the plane's failure and requested that defendant produce the Air Force's post-accident report. At stake was the disclosure of hard data about this equipment that the Air Force did not want made public. Had a copy of this hard data circulated among technicians, it would have proved to be harmful to national security. Still, the danger of inadvertent disclosure of such "blueprint" material is less than that of "concept" information that is far easier for most people to understand and remember. Concept information is difficult to recoup, as well. "Blueprints" can be tracked and revoked, ideas or concepts cannot.

Evidence sought by the plaintiffs in *Zuckerbraun* and *Bareford* dealt directly with matters most sensitive to the Navy's missile defense systems. The military and state secrets privilege was invoked, and the courts considered whether they could proceed based on nonprivileged information alone. The plaintiffs offered substantial *prima facie* evidence, but their claim depended too heavily on protected information. To proceed without the privileged information would have been pointless because a prerequisite to establishing negligent manufacture, design, and testing of the missile defense system was to obtain the very information the Navy could not impart for security reasons.

Likewise, plaintiffs' superior knowledge claim requires that the parties have access to information that the Air Force cannot impart for security reasons. We have established that it is not proper to

consider plaintiffs' *prima facie* evidence in a vacuum when defendant might refute plaintiffs' evidence with greater access. By its nature, plaintiffs' superior knowledge claim is burdened with information that can never be in evidence.

We are absorbed by the concerns expressed in *Farnsworth* about the temptation for parties to probe as close to privileged information as possible in open court. That court decided that dismissal was appropriate because sensitive matters could not be cordoned off in a safe manner, even under the supervision of a trial judge. The information at stake in the present case is vulnerable to inadvertent disclosure. Notwithstanding plaintiffs' ability to present a *prima facie* case based on A-12 program information alone, the Government's incentive would be to expand the inquiry into other areas to defend itself.

D. Constructive Invocation of the Privilege

The privilege "is not to be lightly invoked. There must be a formal claim of privilege...." *Reynolds*, 345 U.S. at 78, 73 S. Ct. at 532. We do not have a broad formal invocation of the military and state secrets privilege to rely upon in the present case. In July 1993, General Merrill A. McPeak warned the court that matters of national security could be implicated in this litigation, but did not formally invoke the state secrets privilege:

> I have reviewed the determinations of Acting Secretary Donley regarding his invocation of the military and state secrets privilege, and I concur completely in his

assessments and judgments on those matters.

> I have concluded that continued inquiry into what is known as plaintiffs' "superior knowledge" claims would necessarily require examination and use of information that *cannot be disclosed in this litigation.* Litigation of plaintiffs' "superior knowledge" claims would present a continuing threat of disclosure of information for which the military and state secrets privilege has been asserted, *and would present a need for disclosure of additional information over which I would assert the privilege.*

McPeak Decl. at 23 (July 22, 1993) (emphasis supplied). We view this as a decisive statement from the Acting Secretary of the Air Force that further discovery into such matters would compromise national security. It is difficult to conceive of a more thorough and persuasive declaration of the Executive's position than that submitted by General McPeak. And he was not alone in his assessment of the situation. Secretary Donley's declaration explored the potential for unauthorized disclosure to harm national security:

> The United States is the world leader in the production and operation of low observable technology weapons and aircraft. Low observable weapons systems and aircraft have been used in combat, without the loss of United States' life or

> aircraft. We believe that no foreign country presently has either the capability to build low observable aircraft or the capability to develop a credible countermeasure to this technology. The United States has a very limited capability to counter this technology, should it be developed and used against us by a foreign country. Accordingly, inadvertent, unauthorized disclosure of the information that is described in more detail in my *in camera* declaration could severely jeopardize national security.

Donley Decl. at 56 (March 30, 1993). Likewise, Secretary Rice expressed reservations about probing Stealth technology:

> The unauthorized disclosure of the national security information at issue reasonably could be expected to cause *extremely grave damage to the national security*.... If the stealth technology from classified, special access programs, such as the B-2 or F-117A is disclosed without authorization, this will weaken our country's ability to defend itself and could place at risk our aircraft and the lives of the crews of those aircraft.

Rice Decl. at 45 (Nov. 20, 1992) (emphasis supplied).

Invocation of the state secrets privilege can have devastating effects on parties to litigation. For that reason, *Reynolds* erected procedures that protect against improper use of the privilege. A court should not be left to ponder the Executive's intentions; Gen-

eral McPeak has made the Executive's intentions clear.

The absence of a formal claim of privilege ("I hereby invoke the military and state secrets privilege") does not persuade us to reopen superior knowledge discovery to address plaintiffs' equitable adjustment claims. The addition of such words to General McPeak's declaration would not enhance its import. General McPeak issued his declaration as the Acting Secretary of the Air Force. He personally reviewed the materials that caused him concern, and he stated that continued pursuit into plaintiffs' superior knowledge claim was unacceptable. The absence of a formal claim of privilege cannot mean that we should have encouraged the parties to proceed with superior knowledge discovery. General McPeak must have intended his strong words filed with the court to have an effect, however, and to cause some action by the court.

Unauthorized disclosures and questionable use of classification procedures by the Government have added to a general unease about litigating plaintiffs' equitable adjustment claims further. General McPeak's declaration was issued in the wake of the Jeremiah episode. His statement was urgent and clear: further pursuit of plaintiffs' claim would result either in removal of critical information from the case, or unauthorized disclosure. Neither option allows us to proceed.

We have no reason to hesitate in the face of the Executive's request as the trial court did in *Reynolds*. The record before the trial court in *Reynolds*

was not clear enough for it to determine that the plaintiffs were demanding privileged information.

> On the record before the trial court it appeared that this accident occurred to a military plane which had gone aloft to test secret electronic equipment. Certainly there was a reasonable danger that the accident investigation report would contain references to the secret electronic equipment which was the primary concern of the mission.

Of course, even with this information before him, the trial judge was in no position to decide that the report was privileged until there had been a formal claim of privilege. Thus it was entirely proper to rule initially that petitioner had shown probable cause for discovery of the documents.

Reynolds, 345 U.S. at 10, 73 S. Ct. at 533. Thus, the Supreme Court concluded that the trial court was justified in requiring production of the accident report until the privilege was invoked. An engine explosion caused the plane to crash. It may have appeared to the trial court that the electronic equipment on board had little to do with a mechanical engine failure. It was important for the Executive to invoke the privilege formally in *Reynolds*. That is not true of this case.

We are not dealing with a "reasonable danger" that attempts to prove plaintiffs' claims could jeopardize privileged information; such events already have occurred. Plaintiffs' superior knowledge claim requires that attorneys and the court view and use

detailed information about highly sensitive defense programs. "Superior knowledge" demands information concerning who knew what and how they knew it.

Molerio is very different from this case in that a single discrete fact was at issue there. It was not technical information, but an easily understood fact that the court knew to be entirely dispositive of the case. Yet the principles enunciated in *Molerio* inform the action that we take today.

The court in *Molerio* dismissed the case because it was made obvious to the court that plaintiff's constitutional claim was meritless. The public record consisted of facts that appeared to support the plaintiff's argument, but in fact they did not. The privileged information convinced the court that plaintiff's version of the facts was not consistent with reality, so the court refused to allow the case to proceed to trial.

The principle motivating *Molerio* is the court's refusal conduct a sham trial. The court knew the plaintiff's argument had no merit. It would have been an affront to our system of justice to allow the jury to determine facts that bore no relation to reality. The state secrets privilege was formally invoked in *Molerio*, but the court's decision to dismiss the plaintiff's claim did not depend on whether the Executive complied with *Reynolds* procedures. *Molerio* directs the court to dismiss claims that are predicated on a misperception even if the truth is unknown to the plaintiff. It is immaterial how a court becomes aware of the truth. So long as a claimant has assumed a

flawed set of facts, the court should dispose of that claim.[14]

We should not delve further into programs that surround this case to obtain information that may benefit one party or the other.

> It may be possible to satisfy the court, from all the circumstances of the case, that there is a reasonable danger that compulsion of the evidence will expose military matters which, in the interest of national security, should not be divulged. When this is the case, the occasion for the privilege is appropriate, and the court should not jeopardize the security which the privilege is meant to protect by insisting upon an examination of the evidence, even by the judge alone, in chambers.

Reynolds, 345 U.S. at 10, 73 S. Ct. at 533. We cannot know fully the effects that privileged information omitted from evidence would have for the par-

[14] Earlier in this litigation, we were faced with a true *Molerio* type problem. Plaintiffs presented a reasonable claim based on the available facts and circumstances. Defendant objected that the facts available to plaintiffs were misleading and that the truth was contained in classified, non-accessible documents. We reviewed the classified materials *in camera* and verified defendant's argument. The facts upon which plaintiffs premised their claim upon did not reflect reality. If defendant could have explained without endangering national security, it could have presented a complete defense to the claim. We were satisfied that the classified information could not be disclosed under any circumstances. We dismissed the claim without a claim of privilege, and plaintiffs accepted the ruling.

ties in this case. We do know that other low-observable information exists. *Molerio*-type facts may inhabit some of this information, but it would never be a part of this case.

Conducting a trial without a critical dispositive fact would result in a sham. Conducting a trial without numerous layers of potentially dispositive facts has the same result. The situation that we confront is the latter.

We cannot rule on the basis of an incomplete record. The *Molerio* court knew that the plaintiff's claim was insupportable. The record did not reflect this reality, however, and the court was forced to intervene. Here, the relevant facts cannot be obtained in a form that we can use to support a judgment. In a case of this unique nature, we need not know specifics about what information is or will be subject to removal by the Executive; we are satisfied that trying this case would lead to an incomplete record on which rulings by the trial court and consideration by the Federal Circuit on appeal, would be a sham.

CONCLUSION

Every member of this Court is accustomed to hearing complex litigation involving millions of dollars and hundreds of millions of dollars. Such cases are common here and many involve sensitive national secrets. But unique circumstances prevent further trial on the merits of this case. Those circumstances prevent us from ruling on plaintiffs' claim to profits and defendant's claim to a loss adjustment. Information critical to both parties cannot be liti-

gated for reasons stated here, and in the classified appendix.

Limiting plaintiffs' damages to incurred costs and removing defendant's loss ratio from the case spreads the consequences of a difficult and dangerous problem. The Government's defense relies heavily on classified information that would be extremely vulnerable if introduced. The nature of some information makes even peripheral references to it hazardous. Despite everyone's best efforts, the risk of compromising national secrets is too serious to proceed to trial.

The parties have stipulated damages based on our rulings to date. The Clerk will enter judgment in the amount of plaintiffs' incurred costs plus interest upon notice from the court.

IT IS SO ORDERED.

APPENDIX H

United States Court of Federal Claims.

McDONNELL DOUGLAS CORPORATION
and General Dynamics Corporation,
Plaintiffs,

v.

UNITED STATES of America,
Defendant.

No. 91-1204C.

April 8, 1996.

OPINION

HODGES, Judge.

This case comes before the court after almost five years of litigation regarding the termination for default of the A-12. This opinion sets forth our reasons for vacating the termination for default and converting the termination for default decision to a termination for the convenience of the Government.[1]

Plaintiffs McDonnell Douglas Corporation and General Dynamics Corporation contracted with the Navy to develop a carrier-based, low observable (Stealth) attack aircraft known as the A-12.[2]

[1] We adopt the proposed findings of fact issued in the November 5, 1993 Order.

[2] Stealthy characteristics allow aircraft to avoid detection by radar and other forms of observation. The military became very interested in this cutting-edge capability for obvious reasons. The Air Force obtained two stealth aircraft-the B-2 and the F-

Defendant terminated the contract for default on January 7, 1991. Plaintiffs argued that the Navy terminated their contract improperly, and that the contract should be converted to a termination for the convenience of the Government. We tried this part of the case, Count XVII, and later vacated the termination for default:

> Testimony and other evidence at trial showed that the A-12 contract was not terminated because of contractor default. The contract was terminated because the Office of the Secretary of Defense withdrew support and funding from the A-12. Prior to that, the Navy did not believe that the contractors performance justified termination for default.

McDonnell Douglas Corp. and General Dynamics Corp. v. United States, No. 91-1204C, Order, 1994 WL 715992 (Dec. 9, 1994).

Plaintiffs argued that this ruling meant we must convert the termination to one for convenience of the Government immediately; defendant countered that conversion would create a windfall for the contractors if they were in default without excuses as of January 7, 1991. According to defendant, a "technical violation" in terminating the contract

117A; the A-12 was the Navy's attempt at this state-of-the-art technology. The harm to national security if this technology were released could be severely damaging, so the A-12 was treated as a compartmented, special access program. The Navy limited access to those individuals with high-level security clearances who had a need to know this information.

could not justify conversion in light of plaintiffs' alleged "egregious" performance failures. The Navy's failure to exercise discretion in terminating plaintiffs for default was not a technical violation, but we agreed to hear evidence of plaintiffs' egregious conduct. We converted the termination to default to one for the convenience of the Government in December 1995, upon finding that the Navy was aware of all critical information that could have affected a termination decision.

BACKGROUND

The Navy awarded a full-scale engineering and development (FSED) contract to the McDonnell Douglas/General Dynamics team in 1988 after competition in concept development. The incrementally funded, fixed-price incentive FSED contract had a ceiling price of $4,777,330,294 and a target price of $4,379,219,436.[3] Installment payments were scheduled to be obligated over the five-year contract. The Navy obligated a $185,000,000 installment to the contract on November 1, 1990, and a $553,200,000 installment was scheduled for January 7, 1991.

The contractors were to produce eight FSED aircraft. The contract also provided the Navy an option to purchase four production lots of aircraft. Each FSED aircraft would test different characteristics of the A-12; stealth capabilities would

[3] One member of the other team competing for the FSED contract had produced an Air Force bomber with stealthy characteristics. That team would not agree to a fixed-price contract, and its bid exceeded plaintiffs' bid by more than $400 million.

be verified in the "fully capable, fully equipped" eighth aircraft that would serve as the basis for the production lots. Under the original agreement, the first FSED aircraft would be delivered in June 1990; the rest would be delivered monthly through January 1991. The Navy exercised its option on the first production lot on May 31, 1990.

Three design reviews were held during the contract. An initial design review was completed in May 1988 and the Preliminary Design Review was completed in January 1989. The Critical Design Review process, to begin after the design is essentially complete, began in June 1990.

A. Problems with Performance

The parties were aware of problems in the performance of this contract, namely controlling the growth of the aircraft weight and meeting the contract schedule. Contracting Officer Michael Mutty knew during early 1990 that the contractors would not meet the June delivery date for the first FSED aircraft, yet he took no action to terminate the contract then. When the contractors did not meet the first flight date in June, Mutty noted serious concern regarding performance and asked plaintiffs for an estimate of when the first aircraft would be delivered.

The contractors proposed a new schedule. They asserted claims for changes to the contract, partly due to impossibility of performance and nondisclosure of superior knowledge. The contractors' estimates showed that the projected costs would exceed the contract ceiling price by $324

million. Negotiations on a new schedule were not successful. On August 17, the Navy unilaterally issued contract modification P00046 setting the date for first flight as December 31, 1991. It did not terminate the contract then.

The projected weight was a concern throughout contract performance.[4] The contractors' Best and Final Offer (BAFO) design proposal for the aircraft had indicated a weight empty for the aircraft. At that weight, the aircraft was predicted to meet needed performance characteristics.

Problems in meeting the BAFO weight surfaced around September 1988. The Contracting Officer believed that the contractors would overcome the problems. In late 1989, the CO was concerned that the BAFO weight would not be possible, but he did not issue a cure notice. The Navy believed that the aircraft's other performance characteristics would meet its needs even if the aircraft were not at the originally predicted weight.

In January 1990, the Navy estimated that the aircraft in the first production lot would weigh 7930 pounds over BAFO.[5] The contractors' estimate was

[4] This was not an unusual concern for a research and development contract to build an aircraft.

[5] The contractors submitted monthly weight and balance status reports estimating the weight of the eighth FSED aircraft. The reports showed the design or production weight of each part of the aircraft. As the design progressed, the weight assigned to each part could change. The status reports reflected the contractors' current view of the weight; the Navy produced its own estimate based on the contractors' reports and the Navy's assessment of the contractors' commitment to weight-reduction

less. The Navy obligated the scheduled payment of $1.05 billion that month. The CO did not issue a cure notice.

B. Major Aircraft Review

The Department of Defense initiated a Major Aircraft Review at the beginning of 1990 to consider its major aircraft programs in light of a diminishing threat and a changing world situation. Its purpose was to decide whether to continue certain programs or to cancel them. The A-12 was included in that review. Secretary of Defense Richard B. Cheney visited the McDonnell Douglas plant in March 1990 as part of the review. There he heard some concerns with production of the aircraft, but he felt fairly confident that the Navy and the contractors could deliver. The conclusions drawn from the review were that the need for the A-12 remained and the Navy should pursue the program. The Secretary reported these results to Congress in April 1990.

Within weeks after his testimony before Congress, the Secretary learned of problems with the A-12. He was informed that the contractors were having schedule and cost problems that would not allow them to perform under the terms of the contract. The Secretary was disturbed by this information because of his recent testimony before Congress. He discussed his concerns with the contractors that summer.

ideas, the technical validity of those ideas, and other subjective conclusions.

C. Acceptability of the A-12

In July 1990, the Navy sought to revalidate the requirements for the A-12 and to reassess its acceptability at the predicted weight of 7930 over BAFO. The question was whether the increased weight of the aircraft would affect the performance characteristics so that the Navy could not accept the aircraft. The answer was No. The aircraft would be acceptable at the increased weight. The Navy's review concluded that the aircraft would meet all operational requirements at BAFO plus 7930 pounds, which was NAVAIR's estimate of the weight of the aircraft when the first squadron would be introduced to the fleet. The report stated:

> [I]t has been determined that the A-12 aircraft, despite a projected weight growth of 7930 pounds by IOC, will continue to satisfy Navy operational requirements and is a suitable aircraft for Fleet use....
>
> * * * * * *
>
> The A-12 meets or exceeds all up-and-away performance requirements and, in every instance, exceeds A-6 carrier suitability performance.

The Joint Chiefs of Staff, through the Joint Requirements Oversight Council (JROC), conducted its own review of the A-12 requirements. The November 1990 JROC report stated:

> In all cases, while the operational requirement is still the goal, the predicted performance is a quantum improvement

> over current capability and is within the operational parameters of the rest of the airwing and satisfies all mission requirements.... There is nothing in these deviations from the original requirement which in the opinion of the JROC affect the fundamental reasons for developing the A-12.

An independent review by the Office of the Secretary of Defense (CSD) concurred that the A-12 program should be pursued. OSD concluded that there was no reason for terminating the A-12 after looking at whether the "technical, schedule, performance, and cost problem risks [were] sufficiently understood and resolved to warrant continuing the program."

D. Beginning of the End

The Navy obligated $185 million in a scheduled payment at the beginning of November. A $553 million installment payment, one of the largest of the contract, was due on January 7, 1991. Long range budget decisions for Congress were due in January.

At the end of November 1990, two reports regarding the handling of the Major Aircraft Review were published. The Navy's November 28 "Beach Report" found that the Program Manager had been unreasonable in his conclusion that the contract could be completed within the contract ceiling price and that he had failed to anticipate a greater risk to the schedule. Several Navy officials, including the Program Manager, were criticized in the report. A Department of Defense Inspector General report

published on November 29 concluded that the nature and extent of the problems with the A-12 were not identified correctly because the review was handled poorly and without following existing control mechanisms.

In his briefing to the President of the United States during the first week of December, the Secretary expressed his disappointment with the Navy's handling of the A-12 and the Major Aircraft Review and promised to "take action to correct the situation." The UnderSecretary of Defense for Acquisition resigned. On December 3, Secretary Cheney stated that there were "serious shortcomings in the program," and he directed the Deputy Secretary of Defense to review the program's status and to report in 10 days.

The A-12 was discussed in a series of meetings in the following days as the Department of Defense decided whether to include certain programs in its budget requests to Congress in January. A Defense Acquisition Board reviewed the A-12 on December 7 and 11, and a Defense Procurement Review Board discussed the A-12 on December 11, 12, and 13.

On December 12, Secretary of the Navy Lawrence Garrett responded to Secretary Cheney's December 3 request for a review of the program. Garrett expressed concerns about the contractors' willingness to perform the contract in accordance with its terms. Secretary Garrett stated: "The Navy also will examine grounds upon which the contract might be terminated consistent with applicable laws and regulations on or before January 5, 1991. We will

provide you our views as to whether the program should be terminated for default."

E. OSD Directs Navy to Issue Cure Notice

Secretary Cheney sent a show cause memorandum to the Navy on Friday, December 14.

> The A-12 program is in serious trouble. The apparent schedule slippage, cost growth and management deficiencies in this program are intolerable. If we cannot spend the taxpayers' money wisely, we will not spend it. Accordingly, I direct you to show cause by January 4, 1991 why the Department should not terminate the A-12 program and pursue other alternatives.

The Navy issued a cure notice to the contractors the following Monday, December 17. Neither the Contracting Officer nor the Navy had planned to issue a cure notice; the timing was dictated by the show cause memorandum from Secretary Cheney.[6] In fact, the Department of Defense General Counsel directed the Navy to issue the cure notice and insisted on including language regarding the

[6] Rear Admiral William R. Morris, the Assistant Commander for Contracts for Naval Air Systems Command, acted as the Contracting Officer during this time. RADM Morris oversaw management issues on thousands of contracts within his office, but he was not involved in daily matters regarding the A-12. He received information on the A-12 from Procurement Contracting Officer Mutty, but he did not know the details of contract performance or the details of the contract specifications. Mutty signed all A-12 documents throughout performance, except for the cure notice and the termination letter.

contractors' failure to meet specifications. The December 17 cure notice stated:

> You are notified that the Government considers your performance ... unsatisfactory. Specifically, you have failed to fabricate parts sufficient to permit final assembly in time to meet the schedule for delivery of FSED aircraft. In addition, you will not deliver the Lot I pilot production aircraft in accordance with the contract schedule. Moreover, your failure to meet specification requirements, such as aircraft weight, jeopardizes the carrier suitability of your design.
>
> These conditions are endangering performance of [the] contract.... Therefore, unless these conditions are cured by 2 January 1991 the Government may terminate for default under the terms and conditions of the default clause of the contract.

The Navy believed that the aircraft would meet operational needs, if not all contract specifications. At the time of the cure notice, the contractors had been negotiating with the Navy and Department of Defense officials for financial relief that would call for a restructuring of the contract, both in its terms and its allocation of costs. The Contracting Officer was awaiting the outcome of Secretary Cheney's decision under Pub. L. 85-804 regarding the

extraordinary relief.[7] Even if 85-804 relief were not granted, the CO wanted the chance to work out the problems within the existing framework of the contract.

The Office of the Secretary of Defense assumed control over determining whether the A-12 should proceed. OSD directed the Secretary of the Navy not to negotiate with the contractors. The new UnderSecretary of Defense for Acquisition, Mr. Donald Yockey, took charge of negotiating with the contractors. The contractors' financial trouble was his primary concern.

The contractors submitted certified claims for equitable adjustments on December 31. Those claims requested an adjustment to the contract price and schedule due to superior knowledge and failure of the Government to cooperate during performance. Also on December 31, the contractors requested flexible progress payments to improve their cash

[7] [T]he President may authorize any department or agency of the Government which exercises functions in connection with the national defense ... to enter into contracts or into amendments or modifications of contracts ... and to make advance payments thereon, without regard to other provisions of law relating to the making, performance, amendment, or modification of contracts, whenever he deems that such action would facilitate the national defense. The authority conferred by this section shall not be utilized to obligate the United States in an amount in excess of $50,000 without approval by an official at or above the level of an Assistant Secretary or his Deputy....

Pub. L. No. 85-804, 72 Stat. 972 (1958). A report justifying those decisions obligating the United States to more than $50,000 must be presented to the President. *Id.*

flow. The contractors responded to the cure notice on January 2 by disputing that they were in default. They contended that the schedule was invalid and the specifications that allegedly they had failed to meet were unachievable.

Admiral Morris attended a briefing for the UnderSecretary of Defense for Acquisition on January 4. In that meeting, the Chief Engineer for the Navy noted that the operational requirements of the A-12 had been revalidated by the Navy and JROC and that the "technical challenges" that remained were typical for this type of development contract. The Chief Engineer believed that the contractors could overcome the technical problems.

F. Cheney Denies 85-804 Relief

On January 5, a Saturday, Secretary Cheney met with the Secretary of the Navy, the UnderSecretary of Defense for Acquisition, the Navy General Counsel, and the Chairman of the Joint Chiefs of Staff to discuss budgets and the A-12. "And there was also this question of whether or not an additional payment [of $553,200,000] would be made to the contractors on the following Monday," according to Secretary Cheney. The Contracting Officer was not present for this discussion.

Secretary Cheney considered three options: (1) Grant 85-804 relief by providing additional funds and changing the terms of the contract, (2) Direct the contractors to perform, or (3) Terminate the A-12. Cheney understood that the Navy wanted to continue the program and force the contractors to perform according to the terms of the contract.

Cheney did not believe that this was reasonable because the contractors had indicated already that they could not meet the current contract.

Other advisers, namely USD(A) Yockey, recommended against both 85-804 relief and the continuation of the program because the contractors were not willing to accept a sufficient loss on the contract. UnderSecretary of Defense for Acquisition Yockey believed that 85-804 would look like a bailout of the contractors. The only alternative Yockey thought appropriate was termination. He wanted to terminate for default immediately, before more funds were obligated.[8]

The Secretary of Defense decided not to grant 85-804 relief. He believed that the natural consequence of his decision not to grant 85-804 relief would be that the program would be cancelled and that the Navy would have to terminate the contract.[9] Cheney

[8] Those facts are not in dispute, though we do not know for certain what Mr. Yockey believed. Mr. Yockey did not testify because all of the parties acknowledged that he remembers virtually nothing about the weekend in question.

[9] Secretary Cheney's own perception of his role in the termination of the A-12 was somewhat unclear. He stated repeatedly in court that his decision with regard to the A-12 was only to deny 85-804 relief. The decision to terminate the contract, according to his trial testimony, was left to the Navy.

> Q: And in fact, your decision was to terminate the contract for default, isn't that right?
>
> A: My decision was to refuse to grant 85-804 relief, with the expectation of having done that that would lead to the cancellation of the program ..., and ... when I decided not to grant 85-804 relief that meant the end of

the program, that the Navy would then be responsible for terminating the contract. And based on everything I had seen up until then, I would have been surprised if they had terminated the contract on any other basis.

In a letter to the President on January 4, 1991, Secretary Cheney focused on his role in assessing the contractors' performance status:

Although I have not yet made a final decision, we may have little choice but to terminate the contract due to the companies' default on the contract obligations.... If I conclude that it is necessary to terminate the A-12 program due to the contractors' failure to perform, the department will pursue other more affordable approaches.

In testimony before the House Armed Services Committee in 1991, Secretary Cheney stated:

> *The A-12, I did terminate.* It was not an easy decision to make because it is an important requirement that we are trying to fulfill. But no one could tell me how much the program was going to cost, even just through the full-scale development phase, or when it would be available. Data that had been presented at one point a few months ago turned out to be invalid and inaccurate. So after agonizing over it, I made a decision to shut down the program. I think it was the right decision. [Emphasis added.]

Months later before the Senate, Secretary Cheney attempted to clarify his position. He only decided not to grant 85-804 relief, which then led to the termination:

> In terms of killing the A-12, technically what happened-it is important for the record to reflect this-I made the decision not to come back to Congress to ask for billions more to bail out the contracts for the particular phase of the A-12 program that we were in. The Navy then made

was not well-versed in government contracts; he was not aware of the procedure or proper bases for terminating a contract. He did not have a working knowledge of the contractors' equitable adjustment claims or their excuses for alleged non-performance. He did not review the claims of the contractors or the Government. His concerns were limited to cost and schedule. Secretary Cheney informed Secretary Garrett later that day of his decision.

G. OSD Withdraws Support

Admiral Morris was called in to meet with Mr. Yockey and other Defense Department officials at

the decision to terminate the contract. Technically, that is what transpired.

In his June 30, 1993 deposition, Secretary Cheney apparently took responsibility for the termination for default decision: "The IG has generally done good work for the Department of Defense. I don't always agree with them, but sometimes they produce good results. In this particular case, *they recommended termination for default, which is what I ultimately did.*" [Emphasis added.] Government counsel presented the Secretary with an errata sheet after his deposition. Cheney agreed that government counsel's suggestions of error more accurately reflected what he believed occurred. Government counsel argued that the alteration to the deposition was proper and that the third sentence in the quoted excerpt should read, "In this particular case, we recommended termination for default which is what we ultimately did." [Emphasis added.] These changes were provided to plaintiffs' counsel the morning of Secretary Cheney's trial testimony.

the Pentagon on Sunday afternoon, January 6. Admiral Morris was unaware of the outcome of the meeting that Secretary Cheney had with Navy officials the day before. In fact, Admiral Morris was scheduled to be on vacation that weekend. His plans changed on Friday afternoon when Mr. Yockey required him to attend the Sunday meeting.

Admiral Morris learned from Mr. Yockey at the meeting that Secretary Cheney would not support 85-804 relief, that Mr. Yockey, as the Under Secretary of Defense for Acquisition, could not support continuation of the program, and that Mr. Yockey would not authorize the expenditure or obligation of any more funds to the program. Yockey's decision was clear to Morris: "I, Yockey, as the milestone decision authority, can no longer support the program because of cost, schedule, performance problems, and I will not authorize the obligation of any additional funds for the program."

Admiral Morris argued for the opportunity to resolve the issues without extraordinary relief under Pub. L. 85-804. He thought that discussions with the contractors were not conclusive, and he did not believe that 85-804 relief was the only way of addressing the issues. He sought an opportunity to provide assurances that the program could be sustained. Mr. Yockey repeated that no additional funds would be obligated.

Admiral Morris was stunned by the meeting with Yockey. He had not anticipated termination of the A-12 contract. Soon after the meeting, he told the Navy's service acquisition representative that he

probably would terminate the contract for default the following day.

Admiral Morris' disappointment was manifest. He told his wife that evening that "it had been a long, tough day and I hadn't been the winner." He called his immediate superior, Admiral Gentz, at home and told him the Secretary of Defense would not grant 85-804 relief and that Yockey would not support the program. Morris hoped that Gentz could encourage the "big guns" in the Fleet to make a last-ditch effort to save the program. If not, Morris said he would have to terminate the contract for default the next day.

Admiral Morris wanted to address the problems that he believed led to OSD's decision.[10] He believed that the plane, even with its deficiencies, would do the job. He was not sure of the timing, cost, and whether the Navy would get everything it wanted, but he planned to discuss those matters with the contractors on Monday morning.

Admiral Morris was left with little time to carry out those intentions. A $553 million progress payment was due to the contractors on Monday. On Sunday afternoon, he contacted NAVAIR legal counsel, Margaret A. Olsen, and told her that he was prepared to terminate the A-12 contract for default the next day. He directed her to prepare a termination for default memorandum. She had not anticipated a termination for default on the A-12.

[10] Morris "felt the heavy responsibility of doing everything that [he] possibly could do to try to reverse [Yockey's] decision."

She suggested that a termination memorandum from an earlier Navy program, the P-7, be used as a "baseline" for the A-12 memorandum because of the short time frame within which to make the decision.[11]

H. Monday Morning Rush

Ms. Olsen began working on the termination memorandum early Monday morning before Admiral Morris arrived. She edited the P-7 termination memorandum on her computer, deleting information that she believed to be peculiar to that contract.[12]

[11] The use of a draft memorandum was not unusual. Ms. Olsen used a draft memorandum written by the P-7 procurement contracting officer in developing the final termination memorandum for the file on the P-7. What was unusual is that the draft memorandum used in preparation of the A-12 termination memorandum for the file was not from Contracting Officer Mutty or from the A-12, but from an entirely different program. Both the A-12 and P-7 were Navy aircraft, but they had distinctly different missions. In fact, defendant attempted to withhold P-7 documents during discovery because the P-7 program was "irrelevant" to this litigation. Admiral Morris and Ms. Olsen had no reservations in relying on this "irrelevant" program for the substance of the termination memorandum for the A-12.

[12] The A-12 termination memorandum includes excerpts from the P-7 memorandum that are not relevant to the A-12. For example:

> Specifically, the team cannot meet the performance requirements of the contract. The team is currently designing the aircraft to have a weight empty 7930 pounds in excess of the guaranteed contract weight empty. *This additional weight precludes the team from meeting contract requirements for takeoff distance, cruise specific range, maximum airspeed and fuel flow,*

Olsen had little information regarding the A-12 at her disposal when preparing the memorandum. She was generally aware of correspondence and conversations that had occurred between the contractors and the Navy. She had not reviewed the contractors' claims, and she had not seen the contractors' response to the cure notice. She directed her staff of attorneys that morning to gather specific information about the A-12. Ms. Olsen did not consult with Admiral Morris about the basis for termination. She did not discuss the termination with the chief engineer, the program manager, or technical personnel.

Morris did not review any A-12 contract documents in preparation for the termination. He did

all of which affect mission capability. [Emphasis supplied.]

The A-12 had no "takeoff distance" requirement because it was a carrier aircraft.

The memorandum focused on the schedule delays in performance, attributing them to the contractors. The paragraph that specifically discussed the amount of delay expected began:

Since June 1990, the team has consistently reported its delays; and the Navy's independent review confirmed that, given the state of the team's development efforts, delivery of aircraft and completion of related contract requirements could occur no sooner than. [sic]

The sentence stops short of a prediction, even though the contractors and the Navy discussed estimations earlier in the year. The Navy had told Secretary Cheney that the first flight date was expected in September 1992.

not consult with technical personnel. He did not review the FAR provisions concerning a decision to terminate for default. His review of documents was limited to those related to the weight of the aircraft, and then only to check whether the number "7930" used in the termination memorandum was correct. He did not review documents related to schedule or specifications. Morris approved the termination memorandum at midday after less than an hour of review.

Morris faced three alternatives: terminate the contract for convenience, terminate the contract for default, or continue the contract. Admiral Morris wanted to continue the contract.[13]

He dismissed the option to continue, however, because Yockey would not release the payment due that day. Morris thought that the failure to release the payment would put the Government in breach of contract. He felt that he had no choice but to terminate. Admiral Morris based the termination on the fault of the contractors because he did not believe that the Navy bore any responsibility for the contractors' perceived inability to achieve the contract specifications or deliver the aircraft on schedule. Absent some fault on the part of the Navy, he believed that he could not terminate for

[13] Admiral Morris testified at trial:

> Q: Under [Yockey's] guidelines, you couldn't do the one thing that you wanted to do, what you told him you wanted to do, and that was continue the contract and negotiate with the contractors, correct?
>
> A: That's correct.

convenience because he believed that action would result in a windfall to the contractors.

The termination letter sent to the contractors stated that they were being terminated for default for an "inability to complete the design, development, fabrication, assembly and test of the A-12 aircraft within the contract schedule and the Team's inability to deliver an aircraft that meets contract requirements." The letter stated that the contractors had

> failed to explain or cure those conditions [noted in the December 17 cure notice], and that the Team is in default of the contract for having failed to make progress and not meeting contract requirements. The A-12 aircraft will not be delivered within the contract schedule nor will it meet the weight guaranty contained within the contract specification.

DISCUSSION

I.

Default termination is a serious matter. It is a drastic sanction that subjects the contractor to forfeiture. *DeVito v. United States*, 188 Ct. Cl. 979, 990, 413 F.2d 1147 (1969).

The Default Clause of a government contract gives the Government the right to terminate a contract. It does not require that the Government "terminate on a finding of bare default, but merely gives the procuring agency discretion to do so." *Sol O. Schlesinger v. United States*, 182 Ct. Cl. 571, 581,

390 F.2d 702 (1968). This discretion must be exercised and exercised reasonably in a decision to terminate a government contract. 182 Ct. Cl. at 581, 390 F.2d 702; *Darwin Construction Co., Inc. v. United States*, 811 F.2d 593, 596 (Fed. Cir. 1987).

The termination clause of the contract cannot be used as a "device" to rid the Government of its contractual responsibilities. That is "an abdication of responsibility which cannot be sanctioned." *Composite Laminates v. United States*, 27 Fed. Cl. 310, 326 (1992) (citing *Schlesinger*, 182 Ct. Cl. at 581, 390 F.2d 702); *see also John A. Johnson Contracting Corp. v. United States*, 132 Ct. Cl. 645, 132 F. Supp. 698 (1955).

Procurement officials must use judgment in deciding whether to terminate a contract for default; they cannot act as "automatons." *Schlesinger*, 182 Ct. Cl. at 581, 390 F.2d 702. If the contracting officer were "improperly influenced by ... anyone else to terminate the contract for default rather than to exercise his own independent judgment in the light of the factors set out in the regulations, it would represent an abdication rather than an exercise of his discretion." *Fairfield Scientific Corp. v. United States*, 222 Ct. Cl. 167, 182, 611 F.2d 854 (1979). The Government must make its decision on the merits of a contractor's performance, considering alleged defaults as well as excuses therefor. The procurement official must assess all of the relevant circumstances of the contract, and not blindly accept directions from others. *Schlesinger*, 182 Ct. Cl. 571, 390 F.2d 702; *see also Jamco Constructors, Inc.*, VABCA Nos. 3516T, 3271, 94-1 B.C.A. ¶ 26,405 at

131,361-362, 1993 WL 393670 (1993), *reconsideration denied*, 94-2 B.C.A. ¶ 26,792, 1994 WL 64186 (1994).

The FAR provides valuable guidance for deciding whether to terminate. First, "the Government shall decide which type of termination action to take ... only after review by contracting and technical personnel, and by counsel, to ensure the propriety of the proposed action." FAR 49.402.3(a) (emphasis supplied).

> The contracting officer shall consider the following factors in determining whether to terminate a contract for default:
>
> (1) The terms of the contract and applicable laws and regulations.
>
> (2) The specific failure of the contractor and the excuses for the failure.
>
> (3) The availability of the supplies or services from other sources.
>
> (4) The urgency of the need for the supplies or services and the period of time required to obtain them from other sources, as compared with the time delivery could be obtained from the delinquent contractor.
>
> (5) The degree of essentiality of the contractor in the Government acquisition program and the effect of a termination for default upon the contractor's capability as a supplier under other contracts.

> (6) The effect of a termination for default on the ability of the contractor to liquidate guaranteed loans, progress payments, or advance payments.
>
> (7) Any other pertinent facts and circumstances.

FAR 49.402-3(f) (emphasis supplied). The Government should consider those factors when deciding whether to terminate for default.[14] Failure to do so is probative evidence that the decision was made precipitously, and without consideration of the relevant circumstances leading to termination for default. *Darwin*, 811 F.2d at 598; *DCX, Inc. v. Perry, Secretary of Defense*, 79 F.3d 132, 135 (Fed. Cir. 1996) ("compliance or noncompliance with section 49.402-3(f) may aid ... court in determining" whether termination for default was improperly made); *Lafayette Coal Company*, ASBCA No. 32,174, 89-3 B.C.A. ¶ 21,963 at 110,482, 1989 WL 74885 (1989) ("Failure to consider one or more of the factors should not invalidate a termination for default where the totality of the circumstances demonstrates a reasonable exercise of discretion any more than mere lip service to the factors should insulate a termination from scrutiny."); *Jamco Constructors*, 94-1 B.C.A. at 131,361

[14] While we emphasize the mandatory language of the regulations, we do not decide this case on that basis. That is, we do not rule that defendant was obliged to consider every FAR factor. Such consideration would have been valuable evidence that defendant did not fail to exercise any discretion. Morris was not permitted to do so. That is the finding of this court: Neither Morris nor anyone else in the Navy was permitted to exercise discretion in terminating this contract.

("The exercise of discretion involves more than a pro forma check off of factors drawn from *FAR* 49.402-3(f).").

The Government's failure to use reasoned discretion when terminating a contract is not a procedural defect that it may correct later. The Court of Claims has refused to sanction such actions. *Schlesinger*, 182 Ct. Cl. at 584, 390 F.2d 702. An improper termination is set aside and the termination for default is converted to a termination for the convenience of the Government. 182 Ct. Cl. at 584, 390 F.2d 702 (proper remedy where the Government abdicates its discretion is to convert the termination for default to one for the convenience of the Government); *see also Darwin*, 811 F.2d at 598 (when a court finds that the contracting officer's default decision was improperly made it will be set aside).

II.

The *Schlesinger* court vacated the termination because it was not issued for contractor default. In that case, "Plaintiff's status of technical default served only as a useful pretext for the taking of action felt to be necessary on other grounds unrelated to the plaintiff's performance...." 182 Ct. Cl. at 583-84, 390 F.2d 702. The Navy and its contracting officer succumbed to pressure to terminate without regard to the circumstances of performance and the contract. In sum, "the Navy simply surrendered its power of choice" in deciding to terminate, and the default termination was improper. *Id.* at 581, 390 F.2d 702. The termination for default was converted to one for the convenience of the Government.

This case is strikingly similar to *Schlesinger*. The procurement in *Schlesinger* was under Congressional scrutiny and there were implications that the contract should be cancelled. Navy officials responded by instructing the contracting officer to terminate the contract if there were no urgent need for the goods. The contracting officer found no urgent need, though the Navy had approved work on the contract until then and had "waived" a missed delivery date only months earlier.[15] With that finding, Navy officials directed the contracting officer to consider the facts and check with legal counsel to determine whether the contract could be terminated for default. When the contracting officer learned that the contractor would not meet the next delivery date, Navy officials instructed him to "[t]erminate contract * * * immediately for default." *Id.* at 578 (so in original).

The Navy could have terminated for convenience, terminated for default, or continued the contract in this case and in *Schlesinger*. Instead, the Navy "acted as if it had no option but to terminate for default (barring all compensation)." *Id.* at 582, 390 F.2d 702. It did not consider excuses for default or whether the termination should be for convenience. Here, and in *Schlesinger*, the agency's actions before termination had not revealed a desire to terminate. The decision to terminate was made hastily without consideration of relevant facts. No one exercised dis-

[15] "Waiver" was not vital to the court's decision except to establish that the Navy had overlooked earlier performance inadequacies. Yet, the Navy terminated immediately when the next delivery date was missed. The sudden change in attitude toward the contractor is most important.

cretion. Both the contracting officer and the agency felt that they had no choice but to terminate for default.

The Navy's surrender of "its power of choice" in dealing with the A-12 is apparent. It had overlooked the contractors' alleged defaults for months. The contractors missed a delivery date for the first FSD aircraft, and the Government excused it with a unilateral contract modification. The contractors reported that they would not meet the Best and Final Offer weight, and the Government determined that the aircraft still would meet operational requirements.[16]

The contracting officer did not contemplate issuing a cure notice in December. The Navy did not believe the contractors' performance justified termination. The show cause memo from the Secretary of Defense's Office set the wheels in motion. Indeed, OSD directed both the timing and the substance of the cure notice.

The termination of this contract was controlled by OSD's directive to issue a cure notice. Admiral Morris' rush to terminate the contract makes sense only in light of OSD's December 15 show cause letter.

[16] This was a research and development contract to provide the Navy with a replacement for the A-6. The Navy wanted an aircraft with the performance characteristics of that plane, but with stealthy capabilities. The "operational requirements" were the goals set for development including performance needs and compatibility with other systems. When the Navy instituted a review of the program to determine whether it wanted to pursue the A-12, it compared the performance capabilities of the A-12 at BAFO plus 7,930 pounds to the operational requirements. The Navy was satisfied that the A-12 would satisfy those goals.

Morris had not contemplated issuing a cure notice until the Navy received that directive. No performance-related event prompted the cure notice.[17] The Navy capitulated. The contractors' alleged, long-standing "defaults" served as the excuse for beginning a termination process.

The decision to terminate for default was dictated by the Office of the Secretary of Defense's representations that it would not support the program. Morris could not proceed with the one option that he felt was appropriate to continue the contract. Admiral Morris and the Navy believed that the aircraft would meet operational requirements. The Navy's actions after the cure notice did not show that it believed the contract should be terminated. Secretary Garrett argued for continuation of performance under the contract at a January 5 meeting. None of the participants except Yockey asserted that the contractors would be unable to develop an aircraft which suited the Navy's operational needs. Yockey's conclusion is insupportable.

The Navy lost all control over the A-12 when the Secretary of Defense's Office took over negotiations with the contractors. OSD's concerns were financial. The contracting officer was left with no discretion whether to terminate the A-12 contract when Mr.

[17] The NAVAIR weight calculation remained constant throughout 1990 despite contractor indications of possible weight growth. The NAVAIR weights branch could have issued another estimate during the year, but did not. Admiral Morris did not question the weight calculation on January 7 other than to review his files to see if that number was correct. Ms. Olsen did not question that number at the time of termination.

Yockey decided that he would no longer support the A-12. In the end, the contract was not terminated because of contractor default. It was terminated because the Office of the Secretary of Defense withdrew support and funding. "[T]he Navy acted as if it had no option but to terminate for default." *Schlesinger*, 182 Ct. Cl. at 582, 390 F.2d 702.

The contracting officer's use of contractor default was based on his general familiarity with the contractors' performance, which previously he had not believed justified a default termination. He did not consult with technical personnel. He did not review the contractors' claims for equitable adjustments. He could not give adequate attention to the claims that may have excused the alleged defaults in that time, especially those involving superior knowledge issues.[18]

Those individuals who prepared the termination memorandum for the file were not informed by the contracting officer of the chosen grounds for termination. The memorandum was cribbed from another program.[19]

The reasons for default termination thrust upon Admiral Morris were faulty. If plaintiffs were in default, this did not require a termination for default a

[18] Information moves slowly in the world of classified, compartmented information. To some it does not move at all.

[19] The Government argues that this is an internal document, and it may be, but the manner in which it was prepared provides evidence of improper termination in the circumstances of this case.

priori.[20] The Government's interests are not necessarily served by such action. A contracting agency must look beyond mere default and consider the interests both of the Government and the contractors. If the contractor's defaults are excusable, the contracting officer cannot terminate for default.

This contracting officer preferred alternatives to termination for the reasons contemplated by the FAR. Influences that he could not resist thwarted his instincts. Neither Admiral Morris nor anyone else in the Navy or OSD reviewed the FAR factors in connection with the decision to terminate. Secretary Cheney was not familiar with the FAR; we have no reason to think that Mr. Yockey was. Admiral Morris knew about the FAR inquiries. The termination memorandum shows that consideration of the FAR factors was nonexistent. The entire termination procedure was *pro forma* at best.

III.

Nothing in *Schlesinger* justifies a different result here. "Such abdication of responsibility [this court has] always refused to sanction where there is administrative discretion under a contract.... This protective rule should have special application for a default-termination which has the drastic consequence of leaving the contractor without any further compensation." 182 Ct. Cl. at 584, 390 F.2d 702 (citations omitted).

[20] Morris' concern for the public fisc, while admirable, could not be the sole basis for concluding that the contract must be terminated for default, thereby placing the weight of a decision to terminate the pro-gram on the contractors.

The Navy acted as if it had no choice but to terminate for default in both cases. The reason for the Navy's dilemma does not matter. What does matter is that the reasons were not contractor performance or default.

The *Schlesinger* court did not base its decision on the contracting officer's failure to exercise his own judgment. Neither do we. The power to terminate may rest with "the Government," but no one in the Government exercised discretion in terminating this contract for default. *Id.* at 583, 390 F.2d 702. Government counsel attempted to distance the Secretary of Defense and his office from the decision to terminate the contract. Their concerns were cost and schedule.

The authority to grant 85-804 relief rests with the Secretary of Defense. The Secretary explained at trial that his action on plaintiffs' 85-804 application did not amount to a termination of the contract. He testified that his decision was not to terminate the contract, but to deny extraordinary relief to the program.

It does not matter whether the Secretary was correct about the scope or effect of his decision. Secretary Cheney did not review the contract, and he did not consider contractor defaults or any reasons that might have excused those defaults. He did not weigh the merits of different types of terminations or the option of going forward. *See Schlesinger*, 182 Ct. Cl. 571, 390 F.2d 702. Perhaps he could have terminated the contract we had no reason to address this issue. We did not consider whether Secretary Cheney or

anyone in his office could have directed the termination for default because the Government offered no individual or entity other than the contracting officer as the decision-maker. In fact, defendant's witnesses disclaimed such a function during trial. Neither the Secretary of Defense nor anyone else in DOD exercised discretion in the process; no consideration of the contract's circumstances occurred. *See* 182 Ct. Cl. at 584, 390 F.2d 702. If the Secretary did terminate the contract, the reason was not for contractor default.

Defendant argues that the role OSD did play in the termination does not nullify the default termination. According to defendant, the termination for default was the "direct consequence of a legitimate exercise of OSD's statutory and regulatory oversight authority; [t]hat the discretion of the contracting officer regarding contract continuation may have been obviated by OSD's actions is of no consequence." In effect, defendant argues that the Secretary's authority overrides all contractual obligations of the United States. This argument suggests that most government contracts are illusory.

Defendant contends that Congress *Construction Corp. v. United States*, 161 Ct. Cl. 50, 55, 314 F.2d 527 (1963), *cert. denied*,375 U.S. 817, 84 S. Ct. 53, 11 L. Ed. 2d 52 (1963), supports this notion. The Court of Claims held in that case:

> [W]hen purely executive functions of a discretionary nature are imposed on a subordinate official of the Government it is an implied condition that his actions

> (before they have become final) are subject to the review and supervision of his superiors if the superior is authorized to intervene in that particular field and does so in time.

The Court in *Congress Construction* assumed without deciding that the Navy was "legally bound to plaintiff to make a good faith attempt" to convince Congress that certain properties should be purchased. The purchase was contingent upon congressional approval, and both parties knew it. The Court speculated that some implied duty might have arisen, but there was no contract. Defendant's reliance on *Congress Construction* is erroneous.

The Secretary of Defense did not want to continue the program. The Navy could have terminated for convenience or continued the contract upon learning of these views.[21] Admiral Morris did not see this as an option because of the cost to the Government. The Navy used alleged defaults that were longstanding issues between the parties that previously it did not believe justified terminating the contract for default.

IV.

The Navy's less harsh position regarding contract specifications specifically, weight during contract performance confirms that the termination for default was improper. The Navy accepted the over-

[21] As in *Schlesinger*, the termination for convenience clause "could have been used to end performance if the Navy thought it well to do so on learning of the Senate committee's views." 182 Ct. Cl. at 584, 390 F.2d 702.

weight condition of the aircraft. It was willing to continue. The contractors in fact did continue for months because no one expected them to meet the BAFO estimate. Yet DoD directed the Navy to include "weight" as a basis for termination in the cure notice. That was a pretext.

The Navy knew in September 1989 that the contractors could not meet the weight predicted in their Best and Final Offer. In October, the Navy encouraged the contractors to stop worrying about weight and focus on manufacture and assembly. The Navy did not threaten to issue a cure notice then.

The Navy determined in May 1990 that the weight would be 7930 pounds over BAFO. It knew that the original predicted weight was unachievable. All the parties did. Yet no cure notice was issued or threatened then. Plaintiffs pursued weight reduction programs vigorously at the Navy's request. No one thought that the contractors would meet the BAFO weight. The Navy's and the contractors' concern was that the weight not continue to increase. "7930 pounds over BAFO" was the benchmark for weight-reduction efforts.

The contractors notified the Navy on June 13 that they could not meet the BAFO estimate. They requested a revision of the contract. This letter documents the contractors' belief that the BAFO weight had been waived. While the BAFO weight still was in effect, no one believed that it could be achieved. The Navy only wanted an aircraft that could meet its operational needs. The contractors continued to perform.

At termination, the Navy had known for at least eight months that the contractors could not meet the BAFO weight, and the Navy accepted it. Its strategy was to maintain the original contract until the end, then exact consideration for the contractors failure to meet the BAFO weight. It did not want to put the contractors in default.

The contractors relied on the Navy's directions to continue performance despite their failure to meet the BAFO weight. The Navy wanted an aircraft that would meet its operational needs, and plaintiffs design did so at 7930 pounds overweight.[22] In response, the contractors no longer strived to meet BAFO weight.

The weight remained stable throughout 1990 according to the Navy, although there were indications from the contractors of potential weight increases. The Navy pressured the contractors during the summer of 1990 to keep the weight growth under 8000 over BAFO. An extra 70 pounds could not have caused great problems with carrier suitability or the

[22] The 7930 figure was the subject of much debate. As discussed earlier, the 7930 estimate was a government number derived from the contractors' monthly weight and balance status reports. From those reports, the Navy assessed the contractors' commitment to certain weight reduction ideas, analyzed the technical validity of those ideas, and made other subjective conclusions. Throughout 1990, the contractors' estimate was almost 1000 pounds less than the Navy number. The Navy's estimate was no more authoritative than the contractors' numbers. The Navy's assessment of carrier suitability would not necessarily have changed with a higher estimate.

Navy's satisfaction with the aircraft's projected performance.[23]

The Navy and the A-12 were under intense scrutiny during the spring and summer of 1990. The Major Aircraft Review had been a disaster, and Secretary Cheney was concerned. One concern was a perceived inability of the contractors to control the weight growth. Weight growth of an aircraft is not unusual in a research and development program, and weight control always has tradeoffs. The tradeoffs in this instance were acceptable. It was the appearance of the inability to control the weight growth that was more damaging to the Navy than the qualitative effects of more weight.

The Navy obligated payment in the fall of 1990, knowing the limitations of the contractors' weight control efforts. At termination, Admiral Morris and NAVAIR had not changed their weight projections for at least a year. The Navy was willing to go forward with the aircraft in that condition and it allowed the contractors to continue performance with that understanding. It was not included in the cure notice until the Department of Defense General Counsel so directed. The Navy cannot support the inclusion of weight in the cure notice as a reason for termination.

[23] The "strike weight" of the aircraft was 79,000 pounds.

V.

A. Post-Hoc Justifications

A termination for default may be justified at trial on other grounds in some circumstances, if the Government exercised discretion in terminating the contract. *See, e.g., Pots Unlimited, Ltd. v. United States*, 220 Ct. Cl. 405, 600 F.2d 790 (1979) (citations omitted) ("[I]t is settled law that a party can justify a termination if there existed at the time an adequate cause, even if then unknown."). For example, if the contracting officer makes a discretionary decision to terminate, but does so for the wrong reason, the termination may be upheld. However, the reason used must have been a non-curable one, so that the contractor would not be prejudiced by the lack of a cure notice. *See College Point Boat Corp. v. United States*, 267 U.S. 12, 45 S. Ct. 199, 69 L. Ed. 490 (1925); *Pots Unlimited*, 220 Ct. Cl. 405, 600 F.2d 790 (violation of contract provision that prohibited sales of pottery on the property); *Joseph Morton Co. v. United States*, 3 Cl. Ct. 120 (1983), *aff'd*,757 F.2d 1273 (Fed. Cir. 1985) (contractor fraud unknown at time of termination); *Quality Granite Construction Co., Inc.*, ASBCA No. 43846, 93-3 B.C.A. ¶ 26,073, 1993 WL 169822 (1993), *aff'd on reconsideration*,94-1 B.C.A. ¶ 26,430, 1993 WL 409998 (1993), *aff'd*, 26 F.3d 138 (Fed. Cir. 1994) (termination for default proper for violations of Davis-Bacon Act unknown at time of termination); *Samuel T. Isaac & Associates, Inc. v. United States*, 7 Cl. Ct. 255 (1985) (criminal conduct unknown at time of termination); *Kelso v. Kirk Bros. Mechanical Contractors*, 16 F.3d 1173 (Fed. Cir. 1994) (violations of Davis-Bacon Act unknown at the time of termina-

tion may subsequently support termination for default).

A cure notice places the contractor on notice of performance deficiencies that the Government believes will endanger the successful completion of the contract.[24] The cure notice allows the contractor to argue that the deficiencies are excused, or to provide reasonable assurances that the problems can be overcome. Thus, a termination for default is improper if the reasons stated for termination are different from the reasons given in the cure notice. *See generally Composite Laminates v. United States*, 27 Fed. Cl. 310 (the contractor must be on adequate notice of the reasons for default termination for the termination to be proper). The Government may not propose reasons for default at trial that the contractor might have cured had it been on notice of the problem during contract performance. The "post hoc" justification exception is limited to those circumstances in which the cure notice could not have been a factor; i.e., where the reason asserted at trial was non-curable.

The contracting officer did not use discretion in deciding whether to terminate the contract. Then, the contracting officer abandoned its remaining opportunity to consider whether the contract should be terminated for default. If he had used discretion, a

[24] If a termination is predicated upon a failure to make progress so as to endanger performance, "the contracting officer shall give the contractor written notice specifying the failure and providing a period of 10 days (or longer period as necessary) in which to cure the failure." FAR 49.402-3(d).

post hoc justification might have been acceptable because a court would have had the benefit of the contracting officer's review of the FAR factors and other considerations that justified termination for default. *See Spread Information Sciences, Inc.*, ASBCA No. 48,438, 96-1 B.C.A. ¶ 27,996, 1995 WL 592785 (1995).

This contract was not terminated for contractor default. We do not have the benefit of a reasoned decision. We do not know what action the contracting officer would have taken had he been permitted to exercise judgment.[25] A termination decision "issued improperly [without the exercise of discretion] ... cannot have the same status as a default-termination which is the fruit of true consideration." *Schlesinger*, 182 Ct. Cl. at 584, 390 F.2d 702.

Contractor default need not end in termination. The Government commonly elects not to terminate a contract that is in technical default, instead granting an extension or contract modification, or waiving the non-compliance. 182 Ct. Cl. at 581, 390 F.2d 702. The question remains whether there would ever be a sufficient reason in light of the Government's failure to exercise discretion for which the contractor should withstand the harsh result of a default termination, especially where the reason is given first during litigation. *See Walsky Construction Company (II)*, ASBCA No. 41,541, 94-2 B.C.A. ¶ 26,698 at 132,784, 1994 WL 43415 (1994) (where the Government abused its discretion in terminating for default, the

[25] Although we do know that this contracting officer's desire was to continue the contract.

Board stated: "Assuming, *arguendo*, that a different technical ground for default, not relied upon by the contracting officer, was established, it would not affect the outcome of this case.").

I. Bare or Technical Default

The *Schlesinger* court agreed that the contractor was in bare or technical default at the time of termination.[26] Even so, the termination for default could not stand: "[T]he default article does not *require* the Government to terminate on finding a bare default but merely gives the procuring agency discretion to do so, and that discretion was not exercised here by the Navy." 182 Ct. Cl. at 581, 390 F.2d 702 (so in original). The court converted the termination for default to one for the convenience of the Government.

The Court's use of the words "technical" and "bare" in *Schlesinger* to describe default in the circumstances of that case is important and appropriate.[27] The contractor missed a delivery date, and al-

[26] That case uses the terms repeatedly. "As the Board found, plaintiff was at least in technical default when his contract was terminated on July 1st. He was required to deliver 15,000 caps by June 30th and did not do so." 182 Ct. Cl. at 580, 390 F.2d 702. "Our difficulty is that the default article does not require the Government to terminate on finding a bare default but merely gives the procuring agency discretion to do so, and that discretion was not exercised here by the Navy." Id. at 581, 390 F.2d 702 (so in original). "We are certain that there have been a great many instances in which the Government has not terminated a contractor in technical default, but has granted an extension or waived the non-compliance." *Id.* at 581, 390 F.2d 702.

[27] These terms are not found in the FAR, but their plain meaning evokes certain images. *Technical* means "marked by a strict legal interpretation," *Webster's New Collegiate Dictionary* 1196

though the product was in production, the Government used that default as an excuse for escaping an unwanted contract.

The contracting officer may decide that a contract should be terminated upon finding the contractor in default. Thus, the Government has the legal right to operate under the default clause for contractor shortcomings, but the court will not allow it to terminate for default when that default is pretextual.

Much of the termination decision depends on the nature of the performance problems, expectations of the outcome, whether the Government will receive its needs even if not within specifications, and other considerations that properly are left to the procuring agency.[28] A technical or bare default may result more often than not in a continuation of the contract. 182 Ct. Cl. at 581, 390 F.2d 702. It may be economical for the Government to receive goods late or slightly off specification than to reprocure or to go without. *DeVito*, 188 Ct. Cl. at 990, 413 F.2d at 1153 (stating

(1977), or "concerned with or making use of technicalities or minute, formal points." *Webster's New World Dictionary* 1373 (3d. ed. 1988). *Bare* means "without embellishment; unadorned; simple; plain" or "no more than; mere." *Webster's New World Dictionary* 110.

[28] Contracting Officer Mutty indicated that the excess weight did not necessarily constitute the grounds for issuing a cure notice: "There are other performance requirements under the contract. You'd have to look at whether or not they were going to meet some of the other performance requirements ..." and "I guess it would depend on the degree to which it was going to be overweight, but just because it would be over-weight, no, we would not automatically terminate."

that the Government is much more interested in production than in litigation).

The extent of the default may affect a contracting officer's decision whether to continue the contract. The greater and more extensive the problems, the less likely it is that a contracting officer would choose to continue the contract. In such circumstances, a termination for default is more likely. The FAR factors might provide reason to continue the contract or take other action. But that decision is one for the contracting officer and the agency to make.

At some point, default could be so extraordinary or egregious that the Government would have no choice but to terminate. Application of discretion would be superfluous because any rational contracting officer would be compelled to terminate for default.[29] At this extreme, any other decision by the

[29] Defendant argued in January 1995 that the Government had a "right to demonstrate that plaintiffs' overwhelming performance failures and defaults, including their repudiation, were material and unexcused, and that they fully justified, *if not required*, the Government's decision to terminate the contract for default." [Emphasis supplied.] In addition, "Plaintiffs apparently contend that they are entitled to the windfall of their convenience termination costs regardless of the actual *egregiousness* of their performance failures...." At a hearing, the Government pleaded that "if the default was, as we believe occurred here, *egregious and overwhelming*, then the ... violation could not have any impact on the decision to terminate for default. In other words, if the default is *so overwhelming*, it's a harmless error problem because *no reasonable contracting officer could have decided to ignore that default.*" [Emphasis added.] The term "egregious" connotes a harshness appropriate in the circumstances of this case. Indeed, only the most outrageous and flagrant of defaults could absolve the government of its wrong-

contracting officer could be an abuse of discretion.[30] Thus, a termination imposed without the benefit of reasoned discretion could be upheld only if contractor performance were so deficient that termination for default was the only possible result.

Facts known to the Navy at the time of termination constituted no more than a technical or bare default, if that. Morris believed that the contractors were in technical default at the time of termination:

> It was my belief that the contractors were technically in default of the contract, and basically, given the choices that I had, termination for convenience, termination for default, or do nothing, given the fact that I did believe they were in technical default of the contract, it would be irresponsible of me thereto to have the taxpayers and the Government pay for the adjudication of a situation where the contractors, through their failure to perform, had caused the default.

Everyone agreed that the plane would not meet the BAFO weight. The amount of excess was of little

ful termination. Defendant indicated in May 1995 that it intended to prove that the contractors' failure to disclose pertinent information regarding current and projected performance would amount to egregious default.

[30] We told the parties before trial on Count XVII that defendant would have the chance to prove that "the contractors' performance was *so deficient* that a decision to terminate this contract on that basis would have been reasonable." June 17, 1993 Order (emphasis added).

importance; the plane was still expected to meet all "operational requirements." There is no indication that any amount of weight growth would have changed the Navy's position. The contracting officer could have terminated the contractors for such problems, but he could have continued the contract and exacted consideration. The Navy was aware of all critical information it needed to make this decision.

Defendant asks us to uphold the termination for reasons that the Navy had at its disposal but did not believe justified termination for default until OSD withdrew funding. Left to its own devices, the Navy would have continued the contract in the face of such deficiencies. The Navy was not permitted this option because of OSD's action.

J. Anticipatory Repudiation

Defendant contends that the contractors repudiated this contract by their repeated failure to provide adequate assurances when requested, and by their indications that they would not perform the contract. Defendant asserts that repudiation is an absolute defense to the wrongful termination irrespective of whether it was asserted at termination.

A contracting officer may terminate a contract for default when there has been a "positive, definite, unconditional, and unequivocable manifestation of intent ... not to render the promised performance when the time fixed ... by the contract shall arrive...." *Cascade Pacific International v. United States*, 773 F.2d 287, 293 (Fed.Cir.1985) (quoted in *United States v. Dekonty Corp.*, 922 F.2d 826, 828 (Fed.Cir.1991)). Refusal to perform may be evidenced by word or

deed, but it must show that the party "absolutely refuses to perform his contract, and before the time arrives for performance distinctly and unqualifiedly communicates that refusal to the other party...." *Dingley v. Oler*, 117 U.S. 490, 499, 6 S. Ct. 850, 29 L. Ed. 984 (1886).

The contractors did not portray a *positive, definite, unconditional*, and *unequivocal* refusal to perform. The Government did not view any of their actions in this manner; no reasonable party to a contract could have. The parties were engaged in various ongoing disputes over the contract. The contractors made clear to the Navy their difficulties with the contract, and the Navy acknowledged them in many respects. Nonetheless, the contractors continued to perform. Negotiations regarding a specific avenue of relief failed. The contracting officer did not believe that the contractors would not perform; he wanted to continue the contract and address the issues with the contractors without extraordinary relief. That avenue was blocked by the Secretary of Defense, not by the contractors.[31] The contractors did not repudiate this contract.[32]

[31] Defendant argues that Admiral Morris hoped that he "could have" negotiated a solution under the contract, implying that the contractors' repudiation prevented this. In fact, Morris could not pursue this because of OSD, not because of the contractors. Morris testified:

> I sought authority at the meeting on the 6th to attempt- my specific thrust was that even though the Secretary had determined that he would not support extraordinary relief under Public Law 85-804, I wanted the authority and permission to try to negotiate a resolution of

CONCLUSION

The decision terminating the contract for default was not proper. This is not a case about the authority of the Secretary of Defense to cancel contracts or programs. The A-12 contract was not terminated be-

> the issues within the boundaries of the contract, without any extraordinary relief. Again, this was our top priority program, I didn't know whether I would be successful at doing that, but given the fact it was so important to the Navy, I wanted to give it a try, and-
>
> ... I did not personally think that the only possible way out of this was extraordinary relief....
>
> I persisted and asked again that I be given an opportunity. [Yockey] heard me out, he considered it, and he reaffirmed for me that he no longer supported the program and that there would be-he would not authorize the release of additional funds.

[32] Anticipatory repudiation might qualify as a post hoc justification if it had occurred because a cure notice would not have been necessary.

> [W]henever there is a positive, definite, unconditional, and unequivocal manifestation of intent ... not to render the promised performance when the time fixed therefor by the contract shall arrive, the contracting officer is not required to go through the useless motions of issuing a preliminary "10-day cure" notice even though the time for performance has not yet arrived, but may terminate forthwith on the ground of anticipatory breach.
>
> *Mission Valve and Pump Co., Div. of Mission Mfg. Co.*, ASBCA Nos. 13552, 13821, 69-2 BCA ¶ 8010 at 37,243, 1969 WL 718 (1969). Defendant indicated in hearings in preparation for trial in 1995 that it did not have evidence in addition to that presented in the Count XVII trial to support anticipatory repudiation. *See* September 14, 1995 Order.

cause of contractor default. The contract was terminated because the Office of the Secretary of Defense withdrew support and funding from the A-12. Prior to that, the Navy did not believe that the contractors performance justified termination for default.

APPENDIX I

United States Court of Federal Claims.

McDONNELL DOUGLAS CORPORATION
and General Dynamics Corporation,
Plaintiffs,

v.

UNITED STATES of America,
Defendant.

No. 91-1204C.

Nov. 1, 1993.

OPINION AND ORDER

HODGES, Judge.

Plaintiffs McDonnell Douglas and General Dynamics contracted with the Navy to develop a low-observable (Stealth) aircraft known as the A-12. Defendant terminated the contract for default. As one defense to the default termination, plaintiffs alleged that defendant breached its duty under the superior knowledge doctrine. During discovery, the United States invoked the state secrets privilege and filed a supplemental declaration by General Merrill A. McPeak describing the risks of litigating plaintiffs' superior knowledge claims. The declaration persuaded us that the superior knowledge claims could not be tried safely.

We ordered termination of discovery in August. This opinion will explain that Order and related

actions of this court, to the extent possible on the public record. Further explanation which may be necessary will be filed under the appropriate classification.

I.

Plaintiffs' contract to build a Stealth airplane was a closely held, unacknowledged military secret at the time it was entered into by the parties. Stealth technology was then and is today protected within compartmented "Special Access Programs." Special Access Programs are reserved for our nation's most sensitive secrets, and they impose stringent security restrictions to safeguard such information to a greater degree than Secret or Top Secret information. *See* Exec. Order No. 12,356, 3 C.F.R. 166, 174 (1983); *see also* 32 C.F.R. § 20001.45 (1993). Information from Special Access Programs may not be disclosed to a person with a Secret or Top Secret clearance unless the appropriate agency has specifically authorized access to the information for that person.

Security measures protecting information in this case are extensive. Plaintiffs are sophisticated corporations whose business is developing highly sensitive technology for the United States. Their experience and discretion in handling even the most sensitive secrets are not questioned by the Government. Members of the litigation teams and court staff possess Top Secret security clearances. The court is assisted by professional security officers who are trained to safeguard classified information. Discovery in this case is protected by elaborate

means under the supervision of the appropriate government agencies. Special Protective Orders control clearance and attorneys' access. To the extent that procedures are available to protect national secrets in a judicial setting, those procedures are in place.

II.

To avoid wasteful litigation over routine discovery disputes, we met regularly with the parties in informal discovery conferences. During one such meeting, an attorney for General Dynamics reported that a request on his behalf for access to certain classified information had been pending with the Government for months. He informed the court that approval of this request for access was necessary to enable an employee of General Dynamics to discuss certain aspects of this case with him. We asked defendant to investigate the extraordinary delay, and instructed security officers assigned to the court to do the same.

A security officer reported that the request for access had been delayed by a member of the Navy's litigation team. The apparent participation of defendant's lawyer in this process was disturbing because security matters and litigation matters were to remain separate to protect the integrity of the litigation. A Protective Order in place prohibited members of defendant's litigation team from participating in matters involving attorney access. We did not pursue this irregularity at the time because counsel for defendant represented that the

request for access had been forwarded to the appropriate officials.

Defendant informed the court that the Air Force was the responsible agency to address the matter, and that it would do so in due course. Later, the Air Force denied the request for access. Defendant provided no explanation for this denial, but its attorneys understood what the Air Force was shielding from plaintiff's counsel.

Because defendant would not explain the denial of access, we requested an explanation from the Air Force. An Air Force security officer provided a general explanation of what classified information was being protected, and why the Air Force had denied plaintiff's request for access. The Air Force had not authorized anyone access to the information for purposes of this litigation. The Navy litigation team had obtained access by other means. [1]

[1] During the deposition of a government witness, defense counsel deliberately elicited classified, compartmented information to further the government's case on the merits. The Air Force had responsibility for this information and had not authorized access to anyone for purposes of this litigation. The seriousness of this security violation required Air Force officials to take extraordinary corrective action.

> Defendant's counsel later argued that unauthorized access to classified information by the Navy's litigation team was of no concern to the court because it was an internal matter for the Executive. The fact is that improper disclosures have threatened the integrity of the litigation, and therefore they are a paramount concern to the court. The Secretary of the Air Force had advised us that such unauthorized disclosures in this litigation

At a hearing to address the access problem, defendant argued that plaintiffs' counsel should propound an interrogatory that would elicit a response containing the information requiring authorized access. Defendant would then refuse to provide the response. After exchanges of a motion to compel and defendant's reply, the parties would argue the matter in due course. That is, plaintiffs' counsel should guess what information their clients sought to communicate to counsel and submit an interrogatory requesting that information before defendant would explain why it was refusing to permit communication from plaintiffs' employees to their counsel.

Plaintiffs counsel could not propound such an interrogatory because he did not know what his client knew. Plaintiff General Dynamics was seeking authorization from the Government to enable its employee to discuss certain aspects of its case with its counsel. Plaintiffs' counsel could not participate effectively in the resolution of this access problem because they did not know the nature of the information being withheld, or why the refusal to authorize the communication unfairly prejudiced their case.[2]

could cause exceptionally grave damage to our nation's security.

[2] The General Dynamics employee filed a classified affidavit summarizing the information he wished to convey to counsel. We reviewed the affidavit *in camera*, and defendant's litigation team reviewed it; plaintiffs' counsel could not.

The result was that plaintiffs could not participate in the adversarial process. *See Ellsberg v. Mitchell*, 709 F.2d 51, 59 (D.C. Cir. 1983) ("Ignorant of what in fact has been withheld, [plaintiffs] are able only to say that 'too much' has been shielded. The tasks of posing and answering more specific questions therefore devolve on us."), *cert. denied*, 465 U.S. 1038, 104 S. Ct. 1316, 79 L. Ed. 2d 712 (1984). However, we did not favor resorting to *ex parte, in camera* procedures. *See, e.g., In re Taylor*, 567 F.2d 1183, 1187-88 (2d Cir. 1977) ("*In camera* proceedings are extraordinary events in the constitutional framework because they deprive the parties against whom they are directed of the root requirements of due process...."); *Phillippi v. CIA*, 546 F.2d 1009, 1013 (D.C. Cir. 1976) (favoring preservation of adversarial process over resorting to in camera examination when resolving issues).

To preserve a semblance of the adversarial process, we asked the Air Force to provide a "modified briefing" to one attorney for each plaintiff. The modified briefing that we contemplated required only that the Air Force explain the situation to plaintiffs' counsel so they would have some understanding of the serious problem which had arisen.

The modified briefing would not have divulged data that might be contained in other Special Access Programs. Rather, we asked the Air Force to segregate certain sensitive information from the less sensitive. We did not believe that providing this modified briefing to two attorneys with Top Secret clearances who had been entrusted with other

Special Access information would endanger national security. *See Northrop Corp. v. McDonnell Douglas Corp.*, 751 F.2d 395, 401 (D.C. Cir. 1984) ("There is no single rule which will determine when disclosure will present a harm to national interests. The grounds for finding such harm will vary from case to case, depending upon the nature of the information at issue, to whom it will be disclosed, and the means available to limit its dissemination."). Acting Secretary of the Air Force Donley would not agree to the modified briefing.

We ruled that defendant could not preclude disclosure of the information unless the Government asserted a privilege permitting it to do so. Defendant had to either permit the contractor's employee to discuss the information with counsel, or invoke a privilege precluding the communication. To preclude the communication, defendant filed a declaration by Acting Secretary Donley formally invoking the state secrets privilege recognized by the Supreme Court in *United States v. Reynolds*, 345 U.S. 1, 73 S. Ct. 528, 97 L. Ed. 727 (1953). The Secretary also executed a classified in camera declaration explaining the need to invoke the privilege. The information is now privileged, and cannot be disclosed to plaintiffs' counsel. *In re United States*, Misc. No. 374 (Fed. Cir. April 30, 1993) [1 F.3d 1251 (table)].

III.

Most courts have held that privileged information should be removed from the case entirely. The issue then is whether the case can proceed without the information. *See, e.g., Bareford v. General Dynamics*

Corp., 973 F.2d 1138, 1141 (5th Cir. 1992); *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 547-48 (2d Cir. 1991); *Ellsberg v. Mitchell*, 709 F.2d at 64-65. We asked plaintiffs to show that they could proceed with the information known to be available. Plaintiffs satisfied the court that they could do so despite the restrictions imposed thus far, albeit with difficulty. Thus, we could not find they were "manifestly unable to make out a *prima facie* case without the requested information." *Ellsberg v. Mitchell*, 709 F.2d at 65.

Defendant then asked for dismissal of plaintiffs' superior knowledge claims because information excluded from the case was inextricably intertwined with the merits, and might contain evidence refuting plaintiffs' *prima facie* case. We continued ruling on the matter pending a showing by defendant that litigating these claims would unfairly prejudice the Government. *McDonnell Douglas Corp. v. United States*, No. 91-1204 (Fed. Cl. June 21, 1993). We also ruled that these claims would not proceed to trial if discovery would pose an unacceptable risk to national security. *Id.*

We could not permit defendant to rely on the mere unavailability of certain information to show prejudice to its case. Defendant was required to show either that the privilege deprived it of a valid defense or that the subject matter of the claims was inseparable from privileged military secrets. *Bareford v. General Dynamics Corp.*, 973 F.2d at 1141. In *Molerio v. FBI*, the defendant "specifically set forth [its defense]" through in camera declarations relating information protected by the

state secrets privilege. 749 F.2d 815, 825 (D.C. Cir. 1984). Defendant's showing in *Molerio* was conclusive. *Id.* In this case, defendant did not make such a showing, so we could not find that plaintiffs' superior knowledge claims must be dismissed for lack of merit, or that invocation of the state secrets privilege deprived defendant of a conclusive defense.

IV.

We urged defendant to make a comprehensive determination of information subject to the state secrets privilege, as in *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d at 548-53 (declaration of Secretary of the Navy Garrett). Such a declaration would have avoided further *in camera* proceedings and detailed examinations of specific military secrets. *McDonnell Douglas v. United States,* No. 91-1204, slip op. at 3 (Fed. Cl. June 21, 1993). Defendant chose not to do so.

Instead, defendant filed the declaration of General Merrill A. McPeak, Acting Secretary of the Air Force. General McPeak described the threat of unauthorized disclosure of military and state secrets, and warned about "the nature and classification" of the information necessary to resolve plaintiffs' superior knowledge claims. The General stated that further litigation "would present a continuing threat of disclosure of information for which the military and state secrets privilege has been asserted, and would present a need for disclosure of additional information over which I would assert the privilege." General McPeak concurred with Acting Secretary Donley's assertion that "[e]ven if the parties and the

Court attempted to take all conceivable precautions, I believe that there is a substantial risk that national security would be threatened by disclosure of these matters, for purposes of this litigation."

We were particularly concerned about General McPeak's assessment that continued litigation of these matters posed an unacceptable risk to national security. General McPeak stated:

> My review of the inquiry which must be made into plaintiffs' 'superior knowledge' claims convinces me that they involve matters that cannot be disclosed in this litigation. For example, the Government would not be able to provide complete answers to the many questions raised ... because such responses would implicate matters for which the military state secrets privilege applies. Relatively straightforward questions concerning plaintiffs' 'superior knowledge' claims asked in depositions, or at trial, would pose unacceptable risks of disclosure of classified, special access information to individuals not authorized to receive such information.

Ironically, defendant's own security lapses have validated General McPeak's concern.

V.

General McPeak's assessment of the risk to national security is dispositive in light of the Federal Circuit's ruling on access to Air Force programs. Discovery of plaintiffs' superior knowledge claims re-

quired access to the Air Force's B-2 (Stealth bomber) and F-117A (Stealth fighter) programs. Secretary of the Air Force Donald Rice restricted plaintiffs' access to only 10 members of plaintiffs' litigation team at one time. When plaintiffs sought permission to add two additional cleared persons who could provide technical assistance, defendant insisted that two persons already cleared (necessarily two of plaintiffs' four attorneys) be "deaccessed" because having more than 10 persons accessed at one time constituted an unacceptable risk to national security. Ten persons could review Stealth secrets at one time, but not 12. In theory, an infinite number of persons would be allowed to see the Stealth secrets, so long as they did so in groups of 10. Defendant offered no explanation for this logical anomaly, and took the position that it was not required to do so. It did not invoke the state secrets privilege.

We sought some rationale for a decision which otherwise seemed definitive of the term "arbitrary." Defendant argued that the Secretary's assessment of what constituted an unacceptable risk to national security was committed to his absolute discretion. The Federal Circuit ruled on this point that Secretary Rice's judgment is not reviewable. *In re United States*, Misc. No. 370, slip op. at 15-16 (Fed. Cir. April 19, 1993) [1 F.3d 1251 (table)]. Therefore, General McPeak's conclusion that litigating this portion of the case would risk our nation's security cannot be questioned by this court.

General McPeak declared: "Litigation of plaintiffs' 'superior knowledge' claims would present a continuing threat of disclosure of information for which the

military and state secrets privilege has been asserted." We understand the rationale for this statement because of information available to the court in camera. While plaintiffs cannot respond to this information, we must hold that further litigation of plaintiffs' superior knowledge claims could reasonably be expected to compromise military secrets. *See, e.g., Fitzgerald v. Penthouse International, Ltd.*, 776 F.2d 1236, 1243 (4th Cir. 1985); *Farnsworth Cannon, Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (en banc).

VI.

We cannot resolve the merits of plaintiffs' superior knowledge claims. The information concealed by the state secrets privilege is such that its effect on the merits is not readily apparent. We ruled that plaintiffs could establish a *prima facie* case, and that privileged information known to this court does not clearly establish that defendant could refute that showing. Existing case law does not provide clear guidance for resolving this issue.

In *Attorney General of the United States v. The Irish People, Inc.*, the trial court erred in dismissing an action "when information which 'might' be relevant [to a defense] is unavailable for discovery." 684 F.2d 928, 951 (D.C. Cir. 1982). The court stated that "even if defendant would normally be entitled to discovery, it does not follow that, if there can be no discovery in the particular case, dismissal is the only choice available to the court." *Id.* at 950. The court listed factors that should be considered in determining what effect invocation of the state secrets privi-

lege should have on the case. *Id.* at 951. Such a balancing of interests may not apply to the circumstances of this case.

Plaintiffs' superior knowledge claims are too complex to be resolved through a selective *ex parte, in camera* examination of evidence. *Cf. Heine v. Raus*, 399 F.2d 785, 791 (4th Cir. 1968). The nature of the information involved likely would preclude the court from finding facts with the degree of certainty that justice requires.

The parties agree that if these claims cannot be litigated for the reasons stated, then the party bearing the burden of proof on the superior knowledge issue cannot prevail. Plaintiffs contend that defendant terminated the contract for default, so defendant bears the burden of showing that it did not breach its duty under the superior knowledge doctrine. Plaintiffs made a colorable claim that the duty applies in the circumstances of this case, and they had available the means to make a *prima facie* showing. Defendant responds that the Government cannot be penalized for invoking the state secrets privilege to protect sensitive matters in litigation, and that the superior knowledge claims must be dismissed.

The parties disagree on the question of where the burden of proof lies. No cases addressing this issue have been cited to date.

CONCLUSION

The parties will address the following issues:

1. Whether we should remove counts VI through XI from the case to the extent that

they rely on the allegation that defendant breached its duty under the superior knowledge doctrine;

2. Whether we should make findings regarding the manner in which defendant controlled access to classified information prior to invocation of the state secrets privilege by Acting Secretary Donley; and

3. Whether we should enter judgment for plaintiffs if defendant's invocation of the state secrets privilege precludes them from litigating their superior knowledge claims.

Briefs will be filed concurrently no later than November 19, 1993.

APPENDIX J

NOTE: This order is nonprecedential

United States Court of Appeals,
Federal Circuit.

McDONNELL DOUGLAS CORPORATION,
Plaintiff-Appellant,

and

General Dynamics Corporation,
Plaintiff-Appellant,

v.

UNITED STATES,
Defendant-Appellee.

Nos. 2007-5111, 2007-5131.

ORDER

A combined petition for panel rehearing and for rehearing en banc having been filed by the Appellant,* and a response thereto having been invited by the court and filed by the Appellee,** and the petition for rehearing and response, having been referred to the panel that heard the appeal, and thereafter the petition for rehearing en banc and response having been referred to the circuit judges who are in regular active service,

* Appellant General Dynamics Corporation.

** The court granted leave to General Dynamics to file a reply. The court also granted leave to amicus curiae National Defense Industrial Association to file a brief in support of Appellant's petition.

UPON CONSIDERATION THEREOF, it is

ORDERED that the petition for panel rehearing be, and the same hereby is, DENIED and it is further

ORDERED that the petition for rehearing en banc be, and the same hereby is, DENIED.

The mandate of the court will issue on December 1, 2009.

Circuit Judge Bryson did not participate in the vote.

FOR THE COURT,

/s/Jan Horbaly
Jan Horbaly Clerk

Dated: 11/24/2009

cc: Paul M. Smith,
Charles J. Cooper,
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MCDONNELL DOUGLAS V US, 2007-5111, -5131
(CFC - 91-CV-1204)

APPENDIX K

41 U.S.C. § 605

§ 605. Decision by contracting officer

(a) Contractor claims

All claims by a contractor against the government relating to a contract shall be in writing and shall be submitted to the contracting officer for a decision. All claims by the government against a contractor relating to a contract shall be the subject of a decision by the contracting officer. Each claim by a contractor against the government relating to a contract and each claim by the government against a contractor relating to a contract shall be submitted within 6 years after the accrual of the claim. The preceding sentence does not apply to a claim by the government against a contractor that is based on a claim by the contractor involving fraud. The contracting officer shall issue his decisions in writing, and shall mail or otherwise furnish a copy of the decision to the contractor. The decision shall state the reasons for the decision reached, and shall inform the contractor of his rights as provided in this chapter. Specific findings of fact are not required, but, if made, shall not be binding in any subsequent proceeding. The authority of this subsection shall not extend to a claim or dispute for penalties or forfeitures prescribed by statute or regulation which another Federal agency is specifically authorized to administer, settle, or determine. This section shall

not authorize any agency head to settle, compromise, pay, or otherwise adjust any claim involving fraud.

(b) Review; performance of contract pending appeal

The contracting officer's decision on the claim shall be final and conclusive and not subject to review by any forum, tribunal, or Government agency, unless an appeal or suit is timely commenced as authorized by this chapter. Nothing in this chapter shall prohibit executive agencies from including a clause in government contracts requiring that pending final decision of an appeal, action, or final settlement, a contractor shall proceed diligently with performance of the contract in accordance with the contracting officer's decision.

(c) Amount of claim; certification; notification; time of issuance; presumption

(1) A contracting officer shall issue a decision on any submitted claim of $100,000 or less within sixty days from his receipt of a written request from the contractor that a decision be rendered within that period. For claims of more than $100,000, the contractor shall certify that the claim is made in good faith, that the supporting data are accurate and complete to the best of his knowledge and belief, that the amount requested accurately reflects the contract adjustment for which the contractor believes the government is liable, and that the certifier is duly authorized to certify the claim on behalf of the contractor.

(2) A contracting officer shall, within sixty days of receipt of a submitted certified claim over $100,000--

(A) issue a decision; or

(B) notify the contractor of the time within which a decision will be issued.

(3) The decision of a contracting officer on submitted claims shall be issued within a reasonable time, in accordance with regulations promulgated by the agency, taking into account such factors as the size and complexity of the claim and the adequacy of the information in support of the claim provided by the contractor.

(4) A contractor may request the tribunal concerned to direct a contracting officer to issue a decision in a specified period of time, as determined by the tribunal concerned, in the event of undue delay on the part of the contracting officer.

(5) Any failure by the contracting officer to issue a decision on a contract claim within the period required will be deemed to be a decision by the contracting officer denying the claim and will authorize the commencement of the appeal or suit on the claim as otherwise provided in this chapter. However, in the event an appeal or suit is so commenced in the absence of a prior decision

by the contracting officer, the tribunal concerned may, at its option, stay the proceedings to obtain a decision on the claim by the contracting officer.

(6) The contracting officer shall have no obligation to render a final decision on any claim of more than $100,000 that is not certified in accordance with paragraph (1) if, within 60 days after receipt of the claim, the contracting officer notifies the contractor in writing of the reasons why any attempted certification was found to be defective. A defect in the certification of a claim shall not deprive a court or an agency board of contract appeals of jurisdiction over that claim. Prior to the entry of a final judgment by a court or a decision by an agency board of contract appeals, the court or agency board shall require a defective certification to be corrected.

(7) The certification required by paragraph (1) may be executed by any person duly authorized to bind the contractor with respect to the claim.

(d) Alternative means of dispute resolution

Notwithstanding any other provision of this chapter, a contractor and a contracting officer may use any alternative means of dispute resolution under subchapter IV of chapter 5 of Title 5, or other mutually agreeable procedures, for resolving claims. The contractor shall certify the claim when required to do so as provided under subsection (c)(1) of this section or as otherwise required by law. All

provisions of subchapter IV of chapter 5 of Title 5 shall apply to such alternative means of dispute resolution.

(e) Termination of authority to engage in alternative means of dispute resolution; savings provision

In any case in which the contracting officer rejects a contractor's request for alternative dispute resolution proceedings, the contracting officer shall provide the contractor with a written explanation, citing one or more of the conditions in section 572(b) of Title 5 or such other specific reasons that alternative dispute resolution procedures are inappropriate for the resolution of the dispute. In any case in which a contractor rejects a request of an agency for alternative dispute resolution proceedings, the contractor shall inform the agency in writing of the contractor's specific reasons for rejecting the request.

48 C.F.R. 49.402-3 (current version)

Subpart 49.4. Termination for Default
49.402 Termination of Fixed-Price Contracts for Default.
49.402-3 Procedure for default.

(a) When a default termination is being considered, the Government shall decide which type of termination action to take (i.e., default, convenience, or no-cost cancellation) only after review by

contracting and technical personnel, and by counsel, to ensure the propriety of the proposed action.

(b) The administrative contracting officer shall not issue a show cause notice or cure notice without the prior approval of the contracting office, which should be obtained by the most expeditious means.

(c) Subdivision (a)(1)(i) of the Default clause covers situations when the contractor has defaulted by failure to make delivery of the supplies or to perform the services within the specified time. In these situations, no notice of failure or of the possibility of termination for default is required to be sent to the contractor before the actual notice of termination (but see paragraph (e) below). However, if the Government has taken any action that might be construed as a waiver of the contract delivery or performance date, the contracting officer shall send a notice to the contractor setting a new date for the contractor to make delivery or complete performance. The notice shall reserve the Government's rights under the Default clause.

(d) Subdivisions (a)(1)(ii) and (a)(1)(iii) of the Default clause cover situations when the contractor fails to perform some of the other provisions of the contract (such as not furnishing a required performance bond) or so fails to make progress as to endanger performance of the contract. If the termination is predicated upon this type of failure, the contracting officer shall give the contractor written notice specifying the failure and providing a period of 10

days (or longer period as necessary) in which to cure the failure. When appropriate, this notice may be made a part of the notice described in subparagraph (e)(1) below. Upon expiration of the 10 days (or longer period), the contracting officer may issue a notice of termination for default unless it is determined that the failure to perform has been cured. A format for a cure notice is in 49.607.

(e)(1) If termination for default appears appropriate, the contracting officer should, if practicable, notify the contractor in writing of the possibility of the termination. This notice shall call the contractor's attention to the contractual liabilities if the contract is terminated for default, and request the contractor to show cause why the contract should not be terminated for default. The notice may further state that failure of the contractor to present an explanation may be taken as an admission that no valid explanation exists. When appropriate, the notice may invite the contractor to discuss the matter at a conference. A format for a show cause notice is in 49.607.

(2) When a termination for default appears imminent, the contracting officer shall provide a written notification to the surety. If the contractor is subsequently terminated for default, a copy of the notice of default shall be sent to the surety.

(3) If requested by the surety, and agreed to by the contractor and any assignees, arrangements

may be made to have future checks mailed to the contractor in care of the surety. In this case, the contractor must forward a written request to the designated disbursing officer specifically directing a change in address for mailing checks.

(4) If the contractor is a small business firm, the contracting officer shall immediately provide a copy of any cure notice or show cause notice to the contracting office's small business specialist and the Small Business Administration Regional Office nearest the contractor. The contracting officer should, whenever practicable, consult with the small business specialist before proceeding with a default termination (see also 49.402-4).

(f) The contracting officer shall consider the following factors in determining whether to terminate a contract for default:

(1) The terms of the contract and applicable laws and regulations.

(2) The specific failure of the contractor and the excuses for the failure.

(3) The availability of the supplies or services from other sources.

(4) The urgency of the need for the supplies or services and the period of time required to obtain them from other sources, as compared with the

time delivery could be obtained from the delinquent contractor.

(5) The degree of essentiality of the contractor in the Government acquisition program and the effect of a termination for default upon the contractor's capability as a supplier under other contracts.

(6) The effect of a termination for default on the ability of the contractor to liquidate guaranteed loans, progress payments, or advance payments.

(7) Any other pertinent facts and circumstances.

(g) If, after compliance with the procedures in paragraphs (a) through (f) of this 49.402-3, the contracting officer determines that a termination for default is proper, the contracting officer shall issue a notice of termination stating--

(1) The contract number and date;

(2) The acts or omissions constituting the default;

(3) That the contractor's right to proceed further under the contract (or a specified portion of the contract) is terminated;

(4) That the supplies or services terminated may be purchased against the contractor's account, and that the contractor will be held liable for any excess costs;

(5) If the contracting officer has determined that the failure to perform is not excusable, that the notice of termination constitutes such decision, and that the contractor has the right to appeal such decision under the Disputes clause;

(6) That the Government reserves all rights and remedies provided by law or under the contract, in addition to charging excess costs; and

(7) That the notice constitutes a decision that the contractor is in default as specified and that the contractor has the right to appeal under the Disputes clause.

(h) The contracting officer shall make the same distribution of the termination notice as was made of the contract. A copy shall also be furnished to the contractor's surety, if any, when the notice is furnished to the contractor. The surety should be requested to advise if it desires to arrange for completion of the work. In addition, the contracting officer shall notify the disbursing officer to withhold further payments under the terminated contract, pending further advice, which should be furnished at the earliest practicable time.

(i) In the case of a construction contract, promptly after issuance of the termination notice, the contracting officer shall determine the manner in which the work is to be completed and whether the

materials, appliances, and plant that are on the site will be needed.

(j) If the contracting officer determines before issuing the termination notice that the failure to perform is excusable, the contract shall not be terminated for default. If termination is in the Government's interest, the contracting officer may terminate the contract for the convenience of the Government.

(k) If the contracting officer has not been able to determine, before issuance of the notice of termination whether the contractor's failure to perform is excusable, the contracting officer shall make a written decision on that point as soon as practicable after issuance of the notice of termination. The decision shall be delivered promptly to the contractor with a notification that the contractor has the right to appeal as specified in the Disputes clause.

48 C.F.R. 52.249-2 (current version)

Subpart 52.2. Texts of Provisions and Clauses
52.249-2 Termination for Convenience of the Government (Fixed-Price).

As prescribed in 49.502(b)(1)(i), insert the following clause:

Termination for Convenience of the Government (Fixed-Price) (MAY 2004)

(a) The Government may terminate performance of work under this contract in whole or, from time to time, in part if the Contracting Officer determines that a termination is in the Government's interest. The Contracting Officer shall terminate by delivering to the Contractor a Notice of Termination specifying the extent of termination and the effective date.

(b) After receipt of a Notice of Termination, and except as directed by the Contracting Officer, the Contractor shall immediately proceed with the following obligations, regardless of any delay in determining or adjusting any amounts due under this clause:

(1) Stop work as specified in the notice.

(2) Place no further subcontracts or orders (referred to as subcontracts in this clause) for materials, services, or facilities, except as necessary to complete the continued portion of the contract.

(3) Terminate all subcontracts to the extent they relate to the work terminated.

(4) Assign to the Government, as directed by the Contracting Officer, all right, title, and interest of the Contractor under the subcontracts terminated, in which case the Government shall have the right to settle or to pay any termination

settlement proposal arising out of those terminations.

(5) With approval or ratification to the extent required by the Contracting Officer, settle all outstanding liabilities and termination settlement proposals arising from the termination of subcontracts; the approval or ratification will be final for purposes of this clause.

(6) As directed by the Contracting Officer, transfer title and deliver to the Government (i) the fabricated or unfabricated parts, work in process, completed work, supplies, and other material produced or acquired for the work terminated, and (ii) the completed or partially completed plans, drawings, information, and other property that, if the contract had been completed, would be required to be furnished to the Government.

(7) Complete performance of the work not terminated.

(8) Take any action that may be necessary, or that the Contracting Officer may direct, for the protection and preservation of the property related to this contract that is in the possession of the Contractor and in which the Government has or may acquire an interest.

(9) Use its best efforts to sell, as directed or authorized by the Contracting Officer, any

property of the types referred to in subparagraph (b)(6) of this clause; provided, however, that the Contractor (i) is not required to extend credit to any purchaser and (ii) may acquire the property under the conditions prescribed by, and at prices approved by, the Contracting Officer. The proceeds of any transfer or disposition will be applied to reduce any payments to be made by the Government under this contract, credited to the price or cost of the work, or paid in any other manner directed by the Contracting Officer.

(c) The Contractor shall submit complete termination inventory schedules no later than 120 days from the effective date of termination, unless extended in writing by the Contracting Officer upon written request of the Contractor within this 120-day period.

(d) After expiration of the plant clearance period as defined in subpart 49.001 of the Federal Acquisition Regulation, the Contractor may submit to the Contracting Officer a list, certified as to quantity and quality, of termination inventory not previously disposed of, excluding items authorized for disposition by the Contracting Officer. The Contractor may request the Government to remove those items or enter into an agreement for their storage. Within 15 days, the Government will accept title to those items and remove them or enter into a storage agreement. The Contracting Officer may verify the list upon removal of the items, or if stored, within 45 days from submission of the list, and shall correct the list, as necessary, before final settlement.

(e) After termination, the Contractor shall submit a final termination settlement proposal to the Contracting Officer in the form and with the certification prescribed by the Contracting Officer. The Contractor shall submit the proposal promptly, but no later than 1 year from the effective date of termination, unless extended in writing by the Contracting Officer upon written request of the Contractor within this 1-year period. However, if the Contracting Officer determines that the facts justify it, a termination settlement proposal may be received and acted on after 1 year or any extension. If the Contractor fails to submit the proposal within the time allowed, the Contracting Officer may determine, on the basis of information available, the amount, if any, due the Contractor because of the termination and shall pay the amount determined.

(f) Subject to paragraph (e) of this clause, the Contractor and the Contracting Officer may agree upon the whole or any part of the amount to be paid or remaining to be paid because of the termination. The amount may include a reasonable allowance for profit on work done. However, the agreed amount, whether under this paragraph (f) or paragraph (g) of this clause, exclusive of costs shown in subparagraph (g)(3) of this clause, may not exceed the total contract price as reduced by (1) the amount of payments previously made and (2) the contract price of work not terminated. The contract shall be modified, and the Contractor paid the agreed amount. Paragraph (g) of this clause shall not limit, restrict, or affect the

amount that may be agreed upon to be paid under this paragraph.

(g) If the Contractor and the Contracting Officer fail to agree on the whole amount to be paid because of the termination of work, the Contracting Officer shall pay the Contractor the amounts determined by the Contracting Officer as follows, but without duplication of any amounts agreed on under paragraph (f) of this clause:

(1) The contract price for completed supplies or services accepted by the Government (or sold or acquired under subparagraph (b)(9) of this clause) not previously paid for, adjusted for any saving of freight and other charges.

(2) The total of--

(i) The costs incurred in the performance of the work terminated, including initial costs and preparatory expense allocable thereto, but excluding any costs attributable to supplies or services paid or to be paid under subparagraph (g)(1) of this clause;

(ii) The cost of settling and paying termination settlement proposals under terminated subcontracts that are properly chargeable to the terminated portion of the contract if not included in subdivision (g)(2)(i) of this clause; and

(iii) A sum, as profit on subdivision (g)(2)(i) of this clause, determined by the Contracting Officer under 49.202 of the Federal Acquisition Regulation, in effect on the date of this contract, to be fair and reasonable; however, if it appears that the Contractor would have sustained a loss on the entire contract had it been completed, the Contracting Officer shall allow no profit under this subdivision (iii) and shall reduce the settlement to reflect the indicated rate of loss.

(3) The reasonable costs of settlement of the work terminated, including--

(i) Accounting, legal, clerical, and other expenses reasonably necessary for the preparation of termination settlement proposals and supporting data;

(ii) The termination and settlement of subcontracts (excluding the amounts of such settlements); and

(iii) Storage, transportation, and other costs incurred, reasonably necessary for the preservation, protection, or disposition of the termination inventory.

(h) Except for normal spoilage, and except to the extent that the Government expressly assumed the risk of loss, the Contracting Officer shall exclude from the amounts payable to the Contractor under

paragraph (g) of this clause, the fair value, as determined by the Contracting Officer, of property that is destroyed, lost, stolen, or damaged so as to become undeliverable to the Government or to a buyer.

(i) The cost principles and procedures of part 31 of the Federal Acquisition Regulation, in effect on the date of this contract, shall govern all costs claimed, agreed to, or determined under this clause.

(j) The Contractor shall have the right of appeal, under the Disputes clause, from any determination made by the Contracting Officer under paragraph (e), (g), or (l) of this clause, except that if the Contractor failed to submit the termination settlement proposal or request for equitable adjustment within the time provided in paragraph (e) or (l), respectively, and failed to request a time extension, there is no right of appeal.

(k) In arriving at the amount due the Contractor under this clause, there shall be deducted--

(1) All unliquidated advance or other payments to the Contractor under the terminated portion of this contract;

(2) Any claim which the Government has against the Contractor under this contract; and

(3) The agreed price for, or the proceeds of sale of, materials, supplies, or other things acquired by

the Contractor or sold under the provisions of this clause and not recovered by or credited to the Government.

(l) If the termination is partial, the Contractor may file a proposal with the Contracting Officer for an equitable adjustment of the price(s) of the continued portion of the contract. The Contracting Officer shall make any equitable adjustment agreed upon. Any proposal by the Contractor for an equitable adjustment under this clause shall be requested within 90 days from the effective date of termination unless extended in writing by the Contracting Officer.

(m)(1) The Government may, under the terms and conditions it prescribes, make partial payments and payments against costs incurred by the Contractor for the terminated portion of the contract, if the Contracting Officer believes the total of these payments will not exceed the amount to which the Contractor will be entitled.

(2) If the total payments exceed the amount finally determined to be due, the Contractor shall repay the excess to the Government upon demand, together with interest computed at the rate established by the Secretary of the Treasury under 50 U.S.C. App. 1215(b)(2). Interest shall be computed for the period from the date the excess payment is received by the Contractor to the date the excess is repaid. Interest shall not be charged on any excess payment due to a reduction in the

Contractor's termination settlement proposal because of retention or other disposition of termination inventory until 10 days after the date of the retention or disposition, or a later date determined by the Contracting Officer because of the circumstances.

(n) Unless otherwise provided in this contract or by statute, the Contractor shall maintain all records and documents relating to the terminated portion of this contract for 3 years after final settlement. This includes all books and other evidence bearing on the Contractor's costs and expenses under this contract. The Contractor shall make these records and documents available to the Government, at the Contractor's office, at all reasonable times, without any direct charge. If approved by the Contracting Officer, photographs, microphotographs, or other authentic reproductions may be maintained instead of original records and documents.

(End of clause)

Alternate I (SEP 1996). If the contract is for construction, substitute the following paragraph (g) for paragraph (g) of the basic clause:

(g) If the Contractor and Contracting Officer fail to agree on the whole amount to be paid the Contractor because of the termination of work, the Contracting Officer shall pay the Contractor the amounts determined as follows, but without duplication of any

amounts agreed upon under paragraph (f) of this clause:

(1) For contract work performed before the effective date of termination, the total (without duplication of any items) of--

(i) The cost of this work;

(ii) The cost of settling and paying termination settlement proposals under terminated subcontracts that are properly chargeable to the terminated portion of the contract if not included in subdivision (g)(1)(i) of this clause; and

(iii) A sum, as profit on subdivision (g)(1)(i) of this clause, determined by the Contracting Officer under 49.202 of the Federal Acquisition Regulation, in effect on the date of this contract, to be fair and reasonable; however, if it appears that the Contractor would have sustained a loss on the entire contract had it been completed, the Contracting Officer shall allow no profit under this subdivision (iii) and shall reduce the settlement to reflect the indicated rate of loss.

(2) The reasonable costs of settlement of the work terminated, including--

(i) Accounting, legal, clerical, and other expenses reasonably necessary for the

preparation of termination settlement proposals and supporting data;

(ii) The termination and settlement of subcontracts (excluding the amounts of such settlements); and

(iii) Storage, transportation, and other costs incurred, reasonably necessary for the preservation, protection, or disposition of the termination inventory.

Alternate II (SEP 1996). If the contract is with an agency of the U.S. Government or with State, local, or foreign governments or their agencies, and if the Contracting Officer determines that the requirement to pay interest on excess partial payments is inappropriate, delete subparagraph (m)(2) of the basic clause.

Alternate III (SEP 1996). If the contract is for construction and with an agency of the U.S. Government or with State, local, or foreign governments or their agencies, substitute the following paragraph (g) for paragraph (g) of the basic clause. Subparagraph (m)(2) may be deleted from the basic clause if the Contracting Officer determines that the requirement to pay interest on excess partial payments is inappropriate.

(g) If the Contractor and Contracting Officer fail to agree on the whole amount to be paid the Contractor because of the termination of work, the Contracting

Officer shall pay the Contractor the amounts determined as follows, but without duplication of any amounts agreed upon under paragraph (f) of this clause:

(1) For contract work performed before the effective date of termination, the total (without duplication of any items) of--

(i) The cost of this work;

(ii) The cost of settling and paying termination settlement proposals under terminated subcontracts that are properly chargeable to the terminated portion of the contract if not included in subdivision (g)(1)(i) of this clause; and

(iii) A sum, as profit on subdivision (g)(1)(i) of this clause, determined by the Contracting Officer under 49.202 of the Federal Acquisition Regulation, in effect on the date of this contract, to be fair and reasonable; however, if it appears that the Contractor would have sustained a loss on the entire contract had it been completed, the Contracting Officer shall allow no profit under this subdivision (iii) and shall reduce the settlement to reflect the indicated rate of loss.

(2) The reasonable costs of settlement of the work terminated, including--

(i) Accounting, legal, clerical, and other expenses reasonably necessary for the preparation of termination settlement proposals and supporting data;

(ii) The termination and settlement of subcontracts (excluding the amounts of such settlements); and

(iii) Storage, transportation, and other costs incurred, reasonably necessary for the preservation, protection, or disposition of the termination inventory.

48 C.F.R. 52.249-9 (current version)

Subpart 52.2. Texts of Provisions and Clauses
52.249-9 Default (Fixed-Price Research and Development).

As prescribed in 49.504(b), insert the following clause:

Default (Fixed-Price Research and Development) (APR 1984)

(a)(1) The Government may, subject to paragraphs (c) and (d) below, by written Notice of Default to the Contractor, terminate this contract in whole or in part if the Contractor fails to--

(i) Perform the work under the contract within the time specified in this contract or any extension;

(ii) Prosecute the work so as to endanger performance of this contract (but see subparagraph (a)(2) below); or

(iii) Perform any of the other provisions of this contract (but see subparagraph (a)(2) below).

(2) The Government's right to terminate this contract under subdivisions (1)(ii) and (1)(iii) of this paragraph may be exercised if the Contractor does not cure such failure within 10 days (or more, if authorized in writing by the Contracting Officer) after receipt of the notice from the Contracting Officer specifying the failure.

(b) If the Government terminates this contract in whole or in part, it may acquire, under the terms and in the manner the Contracting Officer considers appropriate, work similar to the work terminated, and the Contractor will be liable to the Government for any excess costs for the similar work. However, the Contractor shall continue the work not terminated.

(c) Except for defaults of subcontractors at any tier, the Contractor shall not be liable for any excess costs if the failure to perform the contract arises from causes beyond the control and without the fault or negligence of the Contractor. Examples of such

causes include (1) acts of God or of the public enemy, (2) acts of the Government in either its sovereign or contractual capacity, (3) fires, (4) floods, (5) epidemics, (6) quarantine restrictions, (7) strikes, (8) freight embargoes, and (9) unusually severe weather. In each instance the failure to perform must be beyond the control and without the fault or negligence of the Contractor.

(d) If the failure to perform is caused by the default of a subcontractor at any tier, and if the cause of the default is beyond the control of both the Contractor and subcontractor, and without the fault or negligence of either, the Contractor shall not be liable for any excess costs for failure to perform, unless the subcontracted supplies or services were obtainable from other sources in sufficient time for the Contractor to meet the required delivery schedule or other performance requirements.

(e) If this contract is terminated for default, the Government may require the Contractor to transfer title and deliver to the Government, as directed by the Contracting Officer, any (1) completed or partially completed work not previously delivered to, and accepted by, the Government and (2) other property, including contract rights, specifically produced or acquired for the terminated portion of this contract. Upon direction of the Contracting Officer, the Contractor shall also protect and preserve property in its possession in which the Government has an interest.

(f) The Government shall pay the contract price, if separately stated, for completed work it has accepted and the amount agreed upon by the Contractor and the Contracting Officer for (1) completed work for which no separate price is stated, (2) partially completed work, (3) other property described above that it accepts, and (4) the protection and preservation of the property. Failure to agree will be a dispute under the Disputes clause. The Government may withhold from these amounts any sum the Contracting Officer determines to be necessary to protect the Government against loss from outstanding liens or claims of former lien holders.

(g) If, after termination, it is determined that the Contractor was not in default, or that the default was excusable, the rights and obligations of the parties shall be the same as if the termination had been issued for the convenience of the Government.

(h) The rights and remedies of the Government in this clause are in addition to any other rights and remedies provided by law or under this contract.

(End of clause)

SUPPLEMENTAL BRIEF

Supreme Court, U.S.
FILED
AUG 20 2013
OFFICE OF THE CLERK

Nos. 09-1298 and 09-1302

In the Supreme Court of the United States

GENERAL DYNAMICS CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

THE BOEING COMPANY, SUCCESSOR TO MCDONNELL DOUGLAS CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether petitioners were automatically entitled to a judicial abrogation of the government's default termination of their contract because the government's unchallenged invocation of the state-secrets privilege precluded litigation of petitioners' claim that their lack of performance was caused by the government's alleged failure to share its superior knowledge.

2. Whether the court of appeals erred in affirming the trial court's determination that the responsible federal contracting officer had acted lawfully in terminating petitioners' contract for default.

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In the Supreme Court of the United States

No. 09-1298

GENERAL DYNAMICS CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

No. 09-1302

THE BOEING COMPANY, SUCCESSOR TO MCDONNELL DOUGLAS CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinions of the court of appeals (Pet. App. 1a-34a, 178a-211a, 250a-279a) are reported at 567 F.3d 1340, 323 F.3d 1006, and 182 F.3d 1319 respectively.[1] The pertinent opinions of the Court of Federal Claims (Pet. App. 35a-177a, 212a-249a, 280a-443a) are reported at 76 Fed.

[1] Unless otherwise specified, all references to the Pet. App. are to the appendix to the petition for a writ of certiorari filed in No. 09-1298.

Cl. 385, 50 Fed. Cl. 311, 40 Fed. Cl. 529, 37 Fed. Cl. 270, 35 Fed. Cl. 358, and 29 Fed. Cl. 791.

JURISDICTION

The judgment of the court of appeals was entered on June 2, 2009. Petitions for rehearing were denied on November 24, 2009 (Pet. App. 444a-445a; 09-1302 Pet. App. 462a-463a). On January 22 and 28, 2010, the Chief Justice extended the time within which to file a petition for a writ of certiorari to and including March 24, 2010, in No. 09-1302 and No. 09-1298 respectively. On March 11 and 12, 2010, the Chief Justice further extended the time to April 23, 2010, and the petitions were filed on that date. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. In January 1988, petitioners entered into a fixed-price incentive contract with the Navy to develop the A-12 Avenger, a new carrier-based attack aircraft employing low-observable (stealth) technology. Pet. App. 2a. The Full Scale Engineering and Development (FSD) contract required petitioners to design, build, and test eight prototype aircraft at a ceiling price of $4,777,330,294. *Ibid.* The contract required petitioners to deliver the first aircraft in June 1990, with subsequent deliveries to be made at specified times ranging from July 1990 to January 1991. *Id.* at 5a. Each of the eight aircraft would be more complex than the last. Testing would be sequential, with later tests dependent upon successful completion of earlier testing. *Id.* at 45a-46a.

From early on, petitioners encountered difficulty in designing and building an aircraft that would meet critical contract specifications within the negotiated schedule. In June 1990, petitioners failed to deliver the first air-

craft as required under the contract. Pet. App. 4a. They informed the government that the estimated cost of performing under the contract would substantially exceed the contract ceiling price, resulting in an estimated cost that was "unacceptable" to them. *Ibid.* Petitioners proposed to address these difficulties by modifying the fixed-price nature of the contract. *Ibid.* The Navy's contracting officer sent petitioners a letter expressing "serious concern" and warning that the failure to meet the first delivery date "could jeopardize performance of the entire [contract] effort." *Ibid.*

In August 1990, because neither petitioner would commit to a schedule without first reaching agreement with the government on outstanding "technical and business" issues (Pet. App. 135a), the government unilaterally modified the contract to extend the delivery dates for all eight aircraft by 18 to 25 months, thereby producing revised delivery dates ranging from December 1991 to February 1993. *Id.* at 5a, 199a-200a. At the time of the modification, petitioners believed they could deliver sooner than the revised schedule required. *Id.* at 225a. Several months later, because of their continuing performance failures, petitioners projected a first delivery date of March 1992 a date in which petitioners themselves soon lost confidence, and which they believed to be achievable "only after significant changes." *Id.* at 5a-6a.

On December 17, 1990, the Navy issued a cure notice informing petitioners that their performance under the contract was "unsatisfactory." Pet. App. 6a. The notice explained that petitioners had "failed to fabricate parts sufficient to permit final assembly in time to meet the schedule for delivery" and had "failed to meet specification requirements." *Id.* at 6a-7a. Because those deficiencies were "endangering performance of [the] contract,"

the Navy informed petitioners that it might terminate the contract for default unless the deficiencies were cured by January 2, 1991. *Id.* at 7a.[2]

In meetings with the government during the next two weeks, petitioners adhered to the position that they could not build the A-12 aircraft for the agreed-upon price, under the agreed-upon schedule, and to the agreed-upon specifications. Pet. App. 7a. Petitioners asserted they could not "get there if [they didn't] change the contract," and that the contract had "to get reformed to a cost type contract or [they could not] do it." *Ibid.* On January 2, 1991, in their formal reply to the cure notice, petitioners reiterated that they would "not meet delivery schedules or certain specifications of the original contract, or the revised FSD delivery schedule." *Ibid.* Petitioners represented that compliance with the Navy's demand to cure the schedule, weight, and other conditions was "unachievable." *Id.* at 7a-8a.

[2] The contract at issue incorporates by reference 48 C.F.R. 52.249-9 (1984) (see Pet. App. 2a-3a), which provides in relevant part:

> (a)(1) The Government may * * * by written Notice of Default to the Contractor, terminate this contract in whole or in part if the Contractor fails to—
>
> (i) Perform the work under the contract within the time specified in this contract or any extension;
>
> (ii) Prosecute the work so as to endanger performance of this contract (but see paragraph (a)(2) below);
>
> * * *
>
> (2) The Government's right to terminate this contract under subdivisions (1)(ii) and (1)(iii) of this paragraph may be exercised if the Contractor does not cure such failure within 10 days (or more, if authorized in writing by the Contracting Officer) after receipt of the notice from the Contracting Officer specifying the failure.

On January 7, 1991, the Navy's contracting officer sent petitioners a letter terminating the contract for default. Pet. App. 8a. The termination letter explained that the action was based on petitioners' inability "to complete the design, development, fabrication, assembly and test of the A-12 aircraft within the contract schedule," as well as their "inability to deliver an aircraft that meets contract requirements," including the "weight guaranty contained within the contract specification." C.A. App. 18,297. Shortly thereafter, the Navy issued a formal demand for the return of unliquidated progress payments totaling $1.35 billion. Pet. App. 8a.

2. In June 1991, petitioners filed suit in the Claims Court (now the Court of Federal Claims (CFC)) under the Contract Disputes Act of 1978 (CDA), 41 U.S.C. 609(a), challenging the default termination on a number of grounds. Petitioners requested, *inter alia*, that the CFC enter a judgment that the government had breached the contract, and that the court convert the termination for default into a termination for convenience. Pet. App. 8a-9a; see Second Am. Unclassified Compl. at 79.[3]

[3] "The right to terminate a contract when there has been no fault or breach by the non-governmental party, that is, for the 'convenience' of the government, appeared as a legal concept after the Civil War, to facilitate putting a speedy end to war production." *Maxima Corp.* v. *United States*, 847 F.2d 1549, 1552 (Fed. Cir. 1988). When a contract is properly terminated for convenience, the contractor ordinarily is entitled to recover "costs incurred, profit on work done and the costs of preparing the termination settlement proposal. Recovery of anticipated profit is precluded." *Ibid.*; see 48 C.F.R. 52.249-2(g). When a contract has been terminated because of an erroneous determination that the contractor was in default, the court may treat the termination as one for the convenience of the government. *Maxima Corp.*, 847 F.2d at 1553.

a. In December 1995, after a trial that focused on petitioners' claim that the Department of Defense had deprived the contracting officer of the ability to make an "independent decision" regarding the termination, the CFC converted the government's termination for default into a termination for convenience. Pet. App. 382a-429a. Although the CFC found that the contracting officer had "based the termination on the fault of the contractors because he did not believe that the Navy bore any responsibility for the contractors' perceived inability to achieve the contract specifications or deliver the aircraft on schedule," it concluded that the termination decision was not the product of "reasoned discretion." *Id.* at 402a, 407a. The CFC did not address the extent of petitioners' performance or whether they had actually been in default of their contractual obligations.

b. Relying on the state-secrets privilege, the CFC dismissed petitioners' claim that the government had caused their performance failures by withholding its "superior knowledge" of classified stealth technology. Pet. App. 343a-381a. The CFC had initially allowed petitioners to pursue discovery on the theory that the government had a duty to provide petitioners at least a "general warning" about problems concerning production of the A-12 aircraft. *Id.* at 354a-355a n.7 (citation omitted). In March 1993, the Acting Secretary of the Air Force invoked the military and state-secrets privilege to protect against disclosure of relevant but sensitive information. *Id.* at 358a. In December 1996, after noting the occurrence of security breaches during the course of the litigation, the CFC determined that petitioners' superior-knowledge claim could not be safely, fairly, or reliably litigated:

> We cannot permit the parties to litigate plaintiffs' equitable adjustment claims for three reasons: (1) One party or the other would be unfairly prejudiced due to limitations placed on discovery by the Executive for national security reasons; (2) Highly classified information may be compromised in discovery despite procedures in place to prevent that from happening; and (3) Even if information available to the parties could be protected properly in discovery, other information necessary for the court to render an honest judgment would not be available.

Id. at 345a.[4]

3. a. In 1999, in its first published opinion in this case, the court of appeals reversed the CFC's initial judgment invalidating the default termination. Pet. App. 250a-279a. The court ruled that the CFC had "erred by vacating the termination for default without first determining whether a default existed." *Id.* at 269a. The court distinguished this case from one involving a pretextual termination, explaining that "[t]he record and the facts found by the trial court establish that the government denied additional funding for the A-12 program and terminated the contract for default because of concerns about contract specifications, contract schedule, and price-factors that are fundamental elements of contract performance." *Ibid.* The court explained that "[b]ecause the trial court focused on the legitimacy of the government's default termination decision, rather than

[4] On the merits, the government argued that petitioners' participation in other classified Air Force programs provided them the information necessary to develop the A-12 aircraft according to specifications. Pet. App. 355a. The CFC found, however, that the privileged nature of the evidence "would lead to an incomplete record" precluding an accurate determination. *Id.* at 380a.

on whether [petitioners] were in fact in default, the parties have not yet been afforded the opportunity to fully litigate default." *Id.* at 278a. The court therefore remanded the case to the CFC to decide whether the default termination was justified. *Ibid.*

b. Without expressing any view on the merits, the court of appeals also vacated the CFC's dismissal of petitioners' superior-knowledge claim, inviting the CFC to reconsider its state-secrets ruling in light of the passage of time and other possible developments. Pet. App. 271a, 278a-279a.

This Court denied petitioners' petition for a writ of certiorari. 529 U.S. 1097 (2000).

4. a. In 2001, after conducting another trial on remand, the CFC sustained the default termination. Pet. App. 212a-249a. The CFC found that petitioners would not have delivered the first aircraft by the revised contractual deadline (December 1991) and therefore were in default of the contract. *Id.* at 218a-228a. The CFC rejected petitioners' various arguments for excusing their default, including their contentions that the revised delivery schedule was unreasonable and therefore unenforceable; that the schedule, even if enforceable, had been waived by the Navy; and that "the contract was impossible to perform." *Id.* at 228a-230a, 246a-248a.

b. The CFC also reaffirmed its prior ruling that petitioners' superior-knowledge claim could not be litigated due to national security concerns. Pet. App. 243a-246a. The CFC found that "the circumstances that prompted the [December 1996] ruling persist." *Id.* at 244a. The CFC added that it was unable to "establish that the information that has been removed from this case would have benefitted either party." *Id.* at 245a.

5. In 2003, in its second published decision, the court of appeals vacated in part and affirmed in part. Pet. App. 178a-211a.

a. The court of appeals affirmed the CFC's determination that the revised delivery schedule imposed by the government was enforceable and had not been waived. Pet. App. 198a-202a. The court nevertheless held that the CFC "did not make adequate findings" to sustain the default termination. *Id.* at 187a. The court explained that although "absolute impossibility of performance or a contractor's complete repudiation or abandonment" is not required, a default termination cannot be justified "based solely on a contractor's concerns about meeting a contractual schedule milestone." *Id.* at 190a. Citing *Lisbon Contractors, Inc.* v. *United States*, 828 F.2d 759, 765 (Fed. Cir. 1987), the court stated that the government must establish a "reasonable belief on the part of the contracting officer that there was no reasonable likelihood that the contractor could perform the entire contract effort within the time remaining for contract performance." Pet. App. 191a. The court again remanded the case to the CFC to make pertinent factual findings and to apply the *Lisbon* standard. *Id.* at 196a-197a.

b. The court of appeals affirmed the CFC's dismissal of petitioners' superior-knowledge claim. Pet. App. 202a-210a. The court held that the government had properly invoked the state-secrets privilege and that the CFC had properly barred litigation of the superior-knowledge claim in light of the attendant risks. *Id.* at 205a-207a. The court also rejected petitioners' contention that, once the state-secret privilege was found to preclude litigation of petitioners' superior-knowledge claim, the Due Process Clause required the CFC to set aside the default termination. The court of appeals relied on this Court's

distinction in *United States* v. *Reynolds*, 345 U.S. 1, 12 (1953), between the government as criminal prosecutor and the government as civil defendant. The court explained that, because petitioners "are the plaintiffs in this purely civil matter, suing the sovereign on the limited terms to which it has consented," the Due Process Clause "does not require that [petitioners] be able to present all defenses, including a defense that would threaten national security." Pet. App. 208a-209a.

6. In 2007, after petitioners declined an opportunity to reopen the trial record (Pet. App. 113a n.54), the CFC again sustained the default termination. *Id.* at 35a-177a. The CFC found that the contract did not specify a date for completion of the entire effort, given that not all the milestone dates had been revised and that the completion date for a research-and-development contract is often indefinite. *Id.* at 70a-74a. The CFC nevertheless determined that the government's revised delivery schedule for the prototypes provided a yardstick that enabled the court "to consider [petitioners'] progress in light of factors that are probative of their ability and willingness to perform." *Id.* at 40a. After considering the record evidence in its totality, the CFC concluded that the government was justified in terminating the contract for failure to make progress. *Id.* at 132a-155a.

7. In 2009, in its third published decision, the court of appeals affirmed. Pet. App. 1a-34a. The court acknowledged that a literal application of the standard announced in *Lisbon* was difficult because the contract at issue here contained no definite completion date. *Id.* at 14a. Like the CFC, however, the court of appeals rejected petitioners' contention that the absence of a completion date categorically precludes the government from terminating a contract for failure to make adequate prog-

ress. *Id.* at 15a. The court relied on *Universal Fiberglass Corporation* v. *United States*, 537 F.2d 393 (Ct. Cl. 1976), a decision cited approvingly in *Lisbon*, see 828 F.2d at 765, in which the Court of Claims (a predecessor to the Federal Circuit) had upheld a default termination for failure to make progress even in the absence of a contract completion date. Pet. App. 16a-17a. The court held that it was possible to apply the *Lisbon* standard in this case based on the totality of the circumstances including the contractor's failure to meet progress milestones, its problems with subcontractors and suppliers, its financial situation, and its performance history (all factors enumerated in its 2003 opinion, see *id.* at 193a-194a)—to determine whether petitioners had failed to "[p]rosecute the work so as to endanger performance" of the contract. *Id.* at 21a (quoting 48 C.F.R. 52.249-9(a)(1)(ii)).

Based on its review of the record, the court of appeals held that the government had satisfied its burden under *Lisbon* of establishing a reasonable belief that there was no reasonable likelihood of timely performance of the contract. Pet. App. 22a-27a. The court noted that petitioners on appeal had presented no argument for excusing their default and no evidence to show that they could have completed the contract on any date without contract restructuring. *Id.* at 28a. The court also rejected petitioners' argument that the default termination could not be sustained because the contracting officer had not conducted the *Lisbon* analysis prior to termination. The court explained that "the government is not required to establish that the contracting officer conducted the analysis necessary to sustain a default." *Id.* at 29a (quoting *Empire Energy Mgmt. Sys., Inc.* v. *Roche*, 362 F.3d 1343, 1357 (Fed. Cir. 2004)). The court further held that the

record evidence established that the contracting officer had exercised reasonable judgment and had not acted arbitrarily in terminating the contract. *Id.* at 30a-32a. In closing, the court reiterated that "the *Lisbon* test remains good law and our conclusion here is dictated by the unique facts of this case." *Id.* at 33a.

ARGUMENT

1. Petitioners do not dispute that the government properly invoked the state-secrets privilege in this case, nor do they challenge the lower courts' determination that the superior-knowledge issue could not be litigated without risking disclosure of secret information. 09-1298 Pet. 14; 09-1302 Pet. 30. Rather, petitioners contend that because the state-secrets privilege barred litigation of their superior-knowledge claim, the lower courts should have automatically entered judgment invalidating the government's default termination. 09-1298 Pet. 13-22; 09-1302 Pet. 28-34. No decision of this Court or any court of appeals supports that contention. Further review is not warranted.

a. The basic legal principles governing the application of the state-secrets privilege are well established and do not appear to be in dispute here. The state-secrets privilege is deeply rooted in both "the law of evidence," *United States* v. *Reynolds*, 345 U.S. 1, 6-7 (1953), and the Executive's "Art[icle] II duties" to protect "military or diplomatic secrets," *United States* v. *Nixon*, 418 U.S. 683, 710 (1974). The government has a "compelling interest" in protecting national-security information, and the responsibility to do so "falls on the President as head of the Executive Branch and as Commander in Chief." *Department of the Navy* v. *Egan*, 484 U.S. 518, 527 (1988).

The state-secrets privilege "belongs to the Government," which must assert it in a "formal claim of privilege, lodged by the head of the department which has control over the matter, after actual personal consideration by that officer." *Reynolds*, 345 U.S. at 7-8 (footnotes omitted). The privilege applies when "there is a reasonable danger that compulsion of the evidence will expose military matters which, in the interest of national security, should not be divulged." *Id.* at 10. While "[t]he court itself must determine whether the circumstances are appropriate for the claim of privilege," it must not in the course of considering that claim "forc[e] a disclosure of the very thing the privilege is designed to protect." *Id.* at 8. When properly invoked, the privilege is absolute: "even the most compelling necessity cannot overcome the claim of privilege if the court is ultimately satisfied that military secrets are at stake." *Id.* at 11.

b. As noted above, petitioners do not challenge the invocation of the state-secrets privilege or the dismissal of their superior-knowledge claim. 09-1298 Pet. 14; 09-1302 Pet. 30. Rather, petitioners contend that, once their superior-knowledge claim had been dismissed, the courts below were required to set aside the default termination. In support of that contention, petitioners rely significantly on the Court's reference in *Reynolds* to lower-court decisions finding it "unconscionable" to allow the government to undertake a criminal prosecution and then invoke its privileges to deprive the accused of his defense. 345 U.S. at 12. Petitioners' current challenge to the default termination, however, cannot properly be analogized to a criminal prosecution brought by the United States.

The government did not file any claim or seek any affirmative relief in the CFC, but rather is the defendant

in a suit commenced by petitioners. This case, moreover, is a civil rather than a criminal proceeding. See Pet. App. 208a. Lower-court decisions requiring the government to forgo criminal prosecution when it invokes certain privileges have "no application in a civil forum where the Government is not the moving party, but is a defendant only on terms to which it has consented." *Reynolds*, 345 U.S. at 12. The CFC proceedings commenced by petitioners are far removed from a criminal prosecution where an accused's liberty is at stake. And while petitioners characterize the government's demand for payment in this case as an attempt to impose "punishment" (09-1298 Pet. 28) or a "civil penalty" (09-1302 Pet. 32), the government simply seeks to recoup (with appropriate interest) monies that it had advanced to petitioners as progress payments for aircraft that it never received.

Among the government's contract rights is the right to terminate a contract for default in appropriate circumstances. See 48 C.F.R. 52.249-9(a) (incorporated by reference into the A-12 contract, see Pet. App. 2a-3a). Under the Tucker Act's waiver of sovereign immunity, 28 U.S.C. 1491(a)(1), and as authorized by the CDA, 41 U.S.C. 609(a), a contractor that is dissatisfied with the government's decision may sue for relief in the CFC. Petitioners' CFC action is thus no different from any other civil suit by a party seeking relief against the United States based on an applicable waiver of sovereign immunity.

Petitioners' characterization of the government as the "moving party" (09-1298 Pet. 16; 09-1302 Pet. 31) in this case is based in part on the fact that default termination has been deemed a "government claim," *Malone* v. *United States*, 849 F.2d 1441, 1443 (Fed. Cir. 1988), for which the government bears the burden of proof under

the CDA, 41 U.S.C. 601 *et seq.* In contract cases as in other litigation, however, the plaintiff may bear the burden of proof on some issues and the defendant on others. Thus, while petitioners bore the burden of proof on the superior-knowledge claim in response to which the government invoked the state-secrets privilege, see *DCX, Inc.* v. *Perry*, 79 F.3d 132, 134 (Fed. Cir.), cert. denied, 519 U.S. 992 (1996); *Koppers Co.* v. *United States*, 405 F.2d 554, 563-564 (Ct. Cl. 1968), the defendant ordinarily bears the burden of proving affirmative defenses. The government here is similarly situated to a private defendant sued for breach of contract after terminating the contract due to the other party's failure to perform or material breach: both bear the burden of justifying the termination based on the plaintiff's non-performance. See E. Allan Farnsworth, 2 *Farnsworth on Contracts* § 8.15, at 509 (3d ed. 2004). But the fact that the defendant bears the burden of proof on that defense does not cause it to be the "moving party" in the litigation.[5]

c. Petitioners also rely (09-1298 Pet. 18; 09-1302 Pet. 32) on decisions of this Court stating that due process principles guarantee a civil defendant "an opportunity to

[5] If the A-12 contract had not required the first progress payment to be made until some date after the government determined that petitioners were in default, the government could simply have declined to make the progress payment (or any other payments) rather than entering a default termination. Petitioners would then have been forced to bring a breach-of-contract action against the government. In such a lawsuit, petitioners clearly would have been plaintiffs and the government the defendant—free to raise petitioners' non-performance as a defense and the state-secrets privilege to rebut any superior-knowledge claim. There is no apparent reason that the timing of progress payments under the contract—the only difference between the hypothetical case and this one should make any substantive difference with respect to the consequences of invoking the state-secrets privilege.

present every available defense." *Lindsey* v. *Normet*, 405 U.S. 56, 66 (1972); *Logan* v. *Zimmerman Brush Co.*, 455 U.S. 422, 429 (1982)). Even putting aside the fact that petitioners are not defendants here (see pp. 13-15, *supra*), those decision do not speak to the application of evidentiary privileges generally or the state-secrets privilege in particular.

This Court's precedents, as well as the Federal Rules of Civil Procedure and Evidence, have long recognized that evidentiary privileges may limit both plaintiffs' and defendants' access to material and may thereby affect a party's ability to prove its case. To further competing public policy interests, the attorney-client privilege, the spousal privilege, the psychotherapist-patient privilege, and the Presidential communications privilege all limit a litigant's access to potentially relevant material. See, *e.g.*, *Upjohn Co.* v. *United States*, 449 U.S. 383, 389 (1981) (attorney-client privilege); *Jaffee* v. *Redmond*, 518 U.S. 1, 10-15 (1996) (psychotherapist-patient privilege); *Trammel* v. *United States*, 445 U.S. 40, 50-52 (1980) (spousal privilege); *Nixon*, 418 U.S. at 708 (Presidential communications privilege); see also Fed. R. Civ. P. 26(b); Fed. R. Evid. 501-502. The lower courts' application of the state-secrets privilege similarly limits petitioners' ability to litigate the superior-knowledge claim in this case. But petitioners cite no civil case in which this Court has deemed the legitimate invocation of a privilege to violate the affected party's due process rights.

Although the courts below rejected petitioners' contention that judgment should automatically be entered in their favor, the CFC afforded petitioners the opportunity to challenge the government's proof that petitioners were in default, and it entertained every argument petitioners sought to present that would not have risked the disclo-

sure of secret information. Neither the Due Process Clause nor this Court's decision in *Reynolds*—which reversed a trial court's automatic finding of negligence against the United States based on the government's invocation of the state-secrets privilege, 345 U.S. at 5—requires the extreme result sought by petitioners. To the contrary, where matters can be fairly litigated without resort to secret information, a suit may continue. *Id.* at 11.

d. Contrary to petitioners' contention (09-1298 Pet. 19-21; 09-1302 Pet. 33-34), the court of appeals' application of the state-secrets privilege does not conflict with decisions of other circuits. Petitioners rely on court of appeals decisions holding that dismissal of a claim is appropriate if invocation of the state-secrets privilege unduly hampers a defendant in establishing a valid defense. See *El-Masri* v. *United States*, 479 F.3d 296, 309-310 (4th Cir.), cert. denied, 552 U.S. 947 (2007); *Tenenbaum* v. *Simonini*, 372 F.3d 776, 777-778 (6th Cir.), cert. denied, 543 U.S. 1000 (2004); *Molerio* v. *FBI*, 749 F.2d 815, 825 (D.C. Cir. 1984); see also *Kasza* v. *Browner*, 133 F.3d 1159, 1166 (9th Cir.), cert. denied, 525 U.S. 967 (1998); *Zuckerbraun* v. *General Dynamics Corp.*, 935 F.2d 544, 547 (2d Cir. 1991). Because petitioners are plaintiffs rather than defendants in this litigation, the court of appeals' decision in this case is fully consistent with the precedents on which petitioners rely. Indeed, the courts below correctly found petitioners' superior-knowledge claim unamenable to adjudication, in part because the state-secrets privilege prevented the government, as the defendant, from effectively responding to that claim. See Pet. App. 367a ("defendant may be unfairly prejudiced if discovery were restricted to these programs"); *id.* at 372a-373a ("it is not proper to consider plaintiffs' *prima*

facie evidence in a vacuum when defendant might refute plaintiffs' evidence with greater access").

Petitioners further suggest (09-1298 Pet. 21; 09-1302 Pet. 32) that federal officials may be tempted to invoke the state-secrets privilege arbitrarily if the government can obtain favorable rulings on issues as to which the privilege has been claimed. As petitioners acknowledge (09-1298 Pet. 20; 09-1302 Pet. 33-34), however, some of the cases on which they rely have culminated in the dismissal of claims against the government after the government's invocation of the state-secrets privilege precluded the assertion of an effective defense. The safeguards against capricious invocation of the state-secrets privilege lie in the procedural and substantive restrictions that this Court has imposed upon the privilege, see *Reynolds*, 345 U.S. at 7-8, 10; p. 13, *supra*, and in the presumption that high-level Executive Branch officials discharge their duties conscientiously and in good faith, not in any prophylactic rule that the government must lose any claim as to which the privilege has been invoked.

The rule that petitioners advocate, moreover, would itself be susceptible to manipulation by private parties. A contractor that challenges the government's termination of a contract for default could raise a superior-knowledge claim simply to induce the government to invoke the state-secrets privilege. Automatic invalidation of the default termination in those circumstances would inappropriately "punish[] [the government] for asserting the privilege." *Salisbury* v. *United States*, 690 F.2d 966, 975 (D.C. Cir. 1982).

There is likewise no sound basis for the speculation of petitioners and their amici that contractors will cease to do business with the government if the court of appeals' decision remains in place. 09-1298 Pet. 21-22;

Chamber of Commerce Amicus Br. 4, 7-8, 16; Nat'l Def. Indus. Assoc. Amicus Br. 5-7, 14, 23-25. The government has a strong interest in attracting contractors to ensure that our Nation's national security and other needs are met. Moreover, contractors like petitioners are highly sophisticated entities that can protect themselves against undue risk in their negotiation of future contracts. The government is not aware of any refusal to deal by contractors, many of whom rely on the government for business, as a result of the court of appeals' decision on the "unique facts of this case." Pet. App. 33a.

2. Petitioners also seek the Court's review of the court of appeals' application of its failure-to-make-progress standard to affirm the CFC's judgment upholding the default termination. Petitioners argue that (a) the contract's lack of a completion date precludes a default termination (09-1302 Pet. i, 37-40); (b) the court of appeals' 2009 decision impermissibly deviated from its 2003 mandate (09-1298 Pet. 31-36); (c) in issuing its 2009 decision, the court of appeals should have remanded again rather than affirm on the existing record (09-1302 Pet. 18-27); and (d) the court of appeals erred in upholding the default termination on grounds not relied on by the contracting officer (09-1298 Pet. 23-31). The lower courts' highly factbound application of the well-established default-termination standard after nearly two decades of litigation—is correct and does not conflict with any decision of this Court or another court of appeals. Further review is not warranted.

a. Petitioner Boeing (09-1302 Pet. i, 37-40) argues that the government can never terminate a contract for failure to make adequate progress if the contract lacks a definite date of completion for all contract performance. Such a per se rule does not comport with the terms of the

default-termination clause, unnecessarily restricts consideration of relevant circumstances, and conflicts with longstanding Federal Circuit precedent.

The federal acquisition regulation, which was incorporated by reference into the A-12 contract (see note 2, *supra*), permits (in relevant part) a default termination when the contractor fails either (i) to "[p]erform the work under the contract within the time specified in this contract or any extension;" or (ii) to "[p]rosecute the work so as to endanger performance of this contract." 48 C.F.R. 52-249-9(a)(1). Although subsection (i) might plausibly be read to require a specific contract completion date, the contracting officer in this case terminated the A-12 contract under subsection (ii) for a failure to prosecute that "endanger[ed] performance of [the] contract." Pet. App. 7a. Nothing in the text of subsection (ii) requires a definite completion date before a determination can be made that the contractor's progress is so inadequate as to call performance into reasonable doubt.

The court of appeals correctly rejected "such a *per se* rule because it serves only the contractors' interest." Pet. App. 20a. Instead, the court examined all the relevant circumstances to determine whether petitioners had failed to make adequate progress so as to justify the default termination under the terms of the provision. See *id.* at 21a ("Only after analyzing the totality of the circumstances can a court determine whether a contractor failed to '[p]rosecute the work so as to endanger performance' of the contract.") (quoting 48 C.F.R. 52.249-9(a)(1)(ii)). The court of appeals relied on the extensive record of petitioners' deficient performance history (including the failure to meet several milestones such as the first delivery date) as well as their financial difficulties (including repeated statements that the con-

tract could not be performed without significant cost restructuring). *Id.* at 22a-27a. Even petitioners appeared to acknowledge that the contract's sequential, "building block" structure made failure to deliver the first aircraft a critical event. See *id.* at 23a (noting petitioners' admission that "one cannot test an aircraft before it has been built, nor build a production airplane before developing its prototype"). The court of appeals correctly held that those facts taken together supported the default termination under the applicable legal standard.

To the extent that petitioners are concerned about an ad hoc factual inquiry into the totality of circumstances for default terminations in contracts that lack a completion date (09-1302 Pet. 34-40), they are free to negotiate completion dates or other metrics into future contracts. As noted above (p. 19, *supra*), contractors like petitioners are highly sophisticated businesses that can adequately protect themselves against any alleged uncertainty created by Federal Circuit precedent. In any event, Boeing's contention (*id.* at 34) that the court of appeals' decision will "[d]estabilize" the law in this area is particularly unavailing because the per se rule that Boeing advocates is itself inconsistent with established Federal Circuit law.

In *Universal Fiberglass Corporation* v. *United States*, 537 F.2d 393, 398 (1976), the Court of Claims (the Federal Circuit's predecessor, whose decisions are binding precedent in that Circuit, see, *e.g.*, *Strickland* v. *United States*, 423 F.3d 1335, 1338 (Fed. Cir. 2005)) sustained a default termination for failure to make progress even though the contract contained no specific completion date. See also *State of Florida, Dep't of Ins.* v. *United States*, 81 F.3d 1093, 1097 (Fed. Cir. 1996) (holding that the Postal Service was justified in terminating a contract for failure to make progress even though the

original deadline for completion had passed and the Postal Service had not set a new one). Indeed, in *Lisbon Contractors, Inc.* v. *United States*, 828 F.2d 759 (Fed. Cir. 1987) a decision that all the parties to this case endorse the court of appeals cited *Universal Fiberglass* approvingly. *Id.* at 765. Although a completion date may facilitate the *Lisbon* analysis, it is not a prerequisite for default termination if the totality of the circumstances indicates that the contractors' failure to make progress makes it reasonably likely that performance would be untimely or not occur at all.[6]

b. Petitioner General Dynamics contends that the court of appeals in its 2009 decision altered the standard articulated in its 2003 opinion, in violation of the "law of the circuit" doctrine (under which ordinarily only an en banc court can overrule a panel decision). 09-1298 Pet. 31-37. In petitioners' view, the standard for default termination articulated in the court's 2003 decision required a contract completion date. *Id.* at 32-33; 09-1302 Pet. 23. Petitioners' argument depends on an unduly narrow parsing of the 2003 opinion. In any event, any refinement in the 2009 opinion in light of new facts on remand does not violate the "law of the circuit" doctrine.

In all three of its published opinions in this case between 1999 and 2009, the court of appeals reaffirmed the *Lisbon* standard embraced by petitioners here. See Pet. App. 15a-16a, 33a, 191a-194a, 269a-270a. To support a default termination under *Lisbon*, "the government must

[6] Boeing suggests in passing (09-1302 Pet. 38) that the court in *Universal Fiberglass* recognized an "exception" to the per se rule Boeing advocates, but it contends that the exception applies only when a contractor is "making no progress at all." The court of appeals, in construing *Universal Fiberglass* more broadly, determined that the record in this case supported its application here. Pet. App. 17a-21a.

establish by a preponderance of the evidence * * * a 'reasonable belief on the part of the contracting officer that there was no reasonable likelihood that the contractor could perform the entire contract effort within the time remaining for contract performance.'" *Id.* at 11a (quoting *id.* at 191a) (citing *Lisbon*, 828 F.2d at 765). All three opinions (like *Lisbon* itself, 828 F.2d at 765) also approvingly cite *Universal Fiberglass*, in which the court upheld a default termination for failure to make progress in the absence of a definite completion date. Pet. App. 16a n.3 (citing *id.* at 194a, 267a). In its 2009 decision, the court of appeals faithfully applied those two established circuit precedents to the facts of this case. *Id.* at 13a-21a.

Petitioners contend (09-1298 Pet. 30; 09-1302 Pet. 23-24) that the court of appeals in its 2009 decision unfairly upset petitioners' expectations by applying a legal standard significantly different from the standard articulated in the court's 2003 opinion. That is incorrect. Although the court in its 2003 opinion directed the CFC on remand to determine the "contract completion date" and the "time remaining for performance" (Pet. App. 196a), the court did not purport to overrule *Universal Fiberglass*, which remained binding precedent within the Federal Circuit and which made clear that a specific completion date is not a prerequisite for a default termination (see pp. 21-22, *supra*).

The court of appeals' 2003 mandate, as reaffirmed in the 2009 decision, required a review of "the evidence and circumstances surrounding the termination" and "the events, actions, and communications leading to the default decision in ascertaining whether the contracting officer had reasonable belief that there was no reasonable likelihood of timely completion." Pet. App. 187a, 195a; see *id.* at 21a. The 2003 opinion specifically identi-

fied relevant factors other than the completion date, including "the contractor's failure to meet progress milestones," "problems with subcontractors and suppliers," its "financial situation," and its "performance history" (*id.* at 193a-194a (citations omitted))—all factors on which the court relied in its 2009 decision in affirming the CFC's subsequent judgment (*id.* at 21a-27a). Indeed, the court in its 2009 decision "reiterate[d] that the *Lisbon* test remains good law and our conclusion here is dictated by the unique facts of this case." *Id.* at 33a.

In any event, because any difference in emphasis between the 2009 and 2003 opinions in the articulation of the *Lisbon* standard was attributable to intervening factual findings by the CFC, the case falls comfortably within an established exception to law-of-the-case doctrine. In *Arizona* v. *California*, 460 U.S. 605, 618 n.8 (1983), this Court recognized that a court may appropriately depart from its own decision in the same case if the prior holding is clearly erroneous and would work a manifest injustice. Contrary to petitioner General Dynamics's contention (09-1298 Pet. 33), other circuits generally follow this Court's guidance in *Arizona* to permit modification of a prior ruling including in light of further record development. See *United States* v. *Wallace*, 573 F.3d 82, 89 (1st Cir.) ("A panel's reconsideration of a ruling made by a previous panel in the same case may be proper if the initial ruling was made on an inadequate record, * * * if newly discovered evidence bears on the question, or if reconsideration would avoid manifest injustice.") (internal quotation marks omitted), cert. denied, 130 S. Ct. 657 (2009); *EEOC* v. *United Ass'n of Journeymen and Apprentices of the Plumbing & Pipefitting*, 235 F.3d 244, 249-250 & n.1 (6th Cir. 2000), cert. denied, 534 U.S. 987 (2001); *Maxfield* v. *Cintas*

Corp., No. 2, 487 F.3d 1132, 1135 (8th Cir. 2007); *Mendenhall* v. *National Transp. Safety Bd.*, 213 F.3d 464, 469 (9th Cir. 2000); *Johnson* v. *Champion*, 288 F.3d 1215, 1226 (10th Cir. 2002); *Murphy* v. *FDIC*, 208 F.3d 959, 966 (11th Cir. 2000); *United States* v. *Thomas*, 572 F.3d 945, 948 (D.C. Cir. 2009), cert. denied, 130 S. Ct. 1725 (2010); cf. *City Pub. Serv. Bd.* v. *General Elec. Co.*, 935 F.2d 78, 82 (5th Cir. 1991).

Petitioner General Dynamics quotes stricter language from Fifth and Ninth Circuit decisions that might appear to foreclose panel reconsideration notwithstanding the *Arizona* exception. See Pet. 09-1298 Pet. 33-34 (quoting *United States* v. *162.20 Acres of Land*, 733 F.2d 377, 379 (5th Cir. 1984), cert. denied, 469 U.S. 1158 (1985); *United States* v. *Washington*, 593 F.3d 790, 798 n.9 (9th Cir. 2010)). The Fifth Circuit's subsequent decision in *City Public Service Board*, however, recognizes that—albeit "[o]nly in extraordinary circumstances" "this court [may] sustain a departure from the 'law of the case' doctrine on the ground that a prior decision was clearly erroneous." 935 F.2d at 82. And the Ninth Circuit's decision in *Mendenhall* applies the *Arizona* exception to vacate an earlier panel ruling that was "clearly erroneous and would work a manifest injustice." 213 F.3d at 469. In any event, defining the precise circumstances under which one Federal Circuit panel may depart from the reasoning of a prior panel in the same case is a function principally entrusted to the Federal Circuit itself. Cf. *Wisniewski* v. *United States*, 353 U.S. 901, 902 (1957) (per curiam) ("It is primarily the task of a Court of Appeals to reconcile its internal difficulties.").

c. Petitioner Boeing contends (09-1302 Pet. 18-27) that the Due Process Clause required the court of appeals to remand the case to the CFC for further fact-

finding under the standard for default termination articulated in the court of appeals' 2009 decision. That contention lacks merit. As explained above (see pp. 22-24, *supra*), the Federal Circuit's 2003 opinion had instructed the CFC to consider substantially the same factors that the court of appeals identified in 2009 in affirming the CFC's ensuing judgment. In any event, although the Federal Circuit may remand to the trial court to apply a newly announced legal standard, *e.g.*, *Baginsky* v. *United States*, 697 F.2d 1070, 1074 (Fed. Cir.), cert. denied, 464 U.S. 981 (1983) such a remand is not required in every case in which the appellate court elaborates on the applicable legal standard. See, *e.g.*, *Pullman-Standard* v. *Swint*, 456 U.S. 273, 292 (1982) (remand is unnecessary where "the record permits only one resolution of the factual issue"); *Hatch* v. *FERC*, 654 F.2d 825, 835 (D.C. Cir. 1981) ("In those cases in which courts have not required the agency to allow the litigants to submit new evidence relevant to the newly announced standard, either actual notice of the operative standard existed at the time of the first hearing, or an additional opportunity to submit evidence was not deemed critical because the agency merely revised the legal significance of the same kind of facts.") (citations omitted).

Boeing's contention (09-1302 Pet. 23) that it "had no reason to anticipate" the relevance of other circumstances underlying its contract performance, and that it therefore lacked a meaningful opportunity to present material evidence, rings hollow in light of this case's long and winding litigation history. The court of appeals first mandated a broad factual inquiry in 1999, which it repeated verbatim in 2003:

> The question of whether Contractors satisfied their duty is of course that of breach, and must be deter-

> mined by taking into account all of the relevant facts and testimony, such as Contractors' statements that they could not meet the contract specifications, the contract delivery schedule, nor complete performance at the specified contract price.

Pet. App. 186a (quoting *id.* at 278a). Petitioners thus were apprised well before 2009 of the relevance of the type of evidence that the court of appeals ultimately invoked in affirming the CFC's judgment.

Accordingly, the court of appeals was well within its discretion in deciding that the extensive factual record compiled over nearly two decades of litigation was sufficiently developed to permit it to apply directly the *Lisbon* standard to this case. Pet. App. 32a ("the facts in the record are sufficient for the court, in a *de novo* review, to sustain the default termination"). In light of the ample evidence the court cited (*id.* at 23a-27a), there is no reason to believe that a third remand to the CFC would have yielded a different result.

d. Petitioner General Dynamics contends (09-1298 Pet. 23) that the court of appeals' application of the *Lisbon* standard "conflict[s] with basic principles of judicial review of administrative action" because the court did not limit itself to the reasons for default termination proffered by the contracting officer. General Dynamics appears to base that argument on the fact that the Federal Circuit upheld the default termination notwithstanding the CFC's statement that "the contracting officer did not conduct a *Lisbon* analysis prior to termination." Pet. App. 29a (quoting *id.* at 176a n.92); see *id.* at 28a-32a. Petitioner's argument lacks merit.

Unlike the court in an Administrative Procedure Act suit, which must sustain a challenged agency decision unless it is unsupported by substantial evidence in the

administrative record, 5 U.S.C. 706, the CFC in a CDA action does not review an administrative record or defer to the contracting officer's decision to terminate for default. See 41 U.S.C. 605(a) ("Specific findings of fact [by the contracting officer] are not required, but, if made, shall not be binding in any subsequent proceeding."); 41 U.S.C. 609(a)(3) (actions challenging contracting officer decisions in the CFC proceed "de novo in accordance with the rules of the * * * court"); cf. *Renegotiation Bd.* v. *Bannercraft Clothing Co.*, 415 U.S. 1, 23 (1974) ("contractor may institute its *de novo* proceeding in the Court of Claims, unfettered by any prejudice from the agency proceeding and free from any claim that the [prior] determination is supported by substantial evidence"). Rather, "the parties start in court * * * with a clean slate," *Wilner* v. *United States*, 24 F.3d 1397, 1402 (Fed Cir. 1994) (en banc), and the CFC decides *de novo*, based on a judicial record, whether the government has satisfied its burden to demonstrate that the default termination was valid. See *Lisbon*, 828 F.2d at 765.

For nearly a century, the government in such a suit has been entitled to establish that a default termination is justified based on any grounds available, regardless of whether those grounds were known at the time of termination. See *College Point Boat Corp.* v. *United States*, 267 U.S. 12, 15-16 (1925) ("A party to a contract who is sued for its breach may ordinarily defend on the ground that there existed, at the time, a legal excuse for nonperformance by him, although he was then ignorant of the fact. He may, likewise, justify an asserted termination, rescission, or repudiation, of a contract by proving that there was, at the time, an adequate cause, although it did not become known to him until later."); see also Pet. App. 29a; *Empire Energy Mgmt. Sys., Inc.* v. *Roche*, 362 F.3d

1343, 1357 (Fed. Cir. 2004) (explaining that "the subjective knowledge of the contracting officer herself is irrelevant" to the proper disposition of a contractor's suit challenging a default termination); *Kelso* v. *Kirk Bros. Mech. Contractors, Inc.*, 16 F.3d 1173, 1175 (Fed. Cir. 1994) ("This court sustains a default termination if justified by circumstances at the time of termination, regardless of whether the Government originally removed the contractor for another reason."); *Joseph Morton Co.* v. *United States*, 757 F.2d 1273, 1277 (Fed. Cir. 1985) ("[I]t is settled law that a party can justify a termination if there existed at the time an adequate cause, even if then unknown.") (quoting *Pots Unlimited, Ltd.* v. *United States*, 600 F.2d 790, 793 (Ct. Cl. 1979)); 2 *Farnsworth* § 8.18, at 526 ("If an injured party terminates, a court will not ask whether the injured party was actually motivated by the other party's breach or even whether the injured party knew of the breach.").[7]

In any event, as the court of appeals explained (Pet. App. 30a-32a), the contracting officer considered several significant deficiencies before deciding to terminate the A-12 contract for default. The contracting officer summarized his reasoning at trial:

> [Petitioners] were in default because they acknowledged they would not be able to achieve the contract specifications and the contract requirements. Two, they had indicated that the[y] would not be able to meet the delivery schedule that was currently in the contract. And three, they would not be able to per-

[7] Petitioner General Dynamics (09-1298 Pet. 25-26) attempts to distinguish these precedents by construing them to permit judicial reliance on new legal, but not factual, justifications for a prior contract termination. As the quotations above indicate, however, those cases do not establish such a distinction.

> form the contract without extraordinary relief or additional funding for the contract. So they basically said they can't perform under the contract and they were in default of it.

Id. at 265a-266a. The contracting officer's conclusion that petitioners would be unable to perform the contract was amply supported by the course of dealing between the parties. For example, when asked in December 1990 by the Under Secretary of Defense whether petitioners would complete the contract regardless of the cost, the CEO of one of the petitioners responded that the contract "has got to get reformed to a cost-type contract or we cannot do it." *Id.* at 81a.

The court of appeals was properly "less concerned about the label of the contracting officer's action so long as, in fulfilling his duty, the contracting officer exercised reasoned judgment and did not act arbitrarily." Pet. App. 30a. The contracting officer's cure notice and termination letter (pp. 3-5, *supra*) substantiate his testimony and support the court's determination that the officer exercised "reasoned judgment" when terminating the contract for default. Pet. App. 30a. Thus, while the contracting officer may not have explicitly conducted a "*Lisbon* analysis" (*id.* at 29a), the rationale on which the officer terminated the contract was not different in kind from the rationale on which the court of appeals upheld the default termination.

CONCLUSION

The petitions for a writ of certiorari should be denied.

Respectfully submitted.

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GENERAL DYNAMICS CORPORATION,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

On Petition For A Writ Of Certiorari To The
United States Court Of Appeals
For The Federal Circuit

REPLY BRIEF ON PETITION FOR WRIT OF CERTIORARI

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INTRODUCTION

In 1988, the Navy entered into a multi-billion-dollar contract with General Dynamics and Boeing to develop and produce the A-12 Avenger, promising to give them access to the government's classified stealth technology. The Navy failed to deliver on that promise. But it recognized that this failure made the contractors' already-challenging task far more difficult – so it changed the original weight specification, disestablished the original schedule, and accepted the contractors' aircraft design.

In 1990, the Secretary of Defense canceled the A-12 program for political reasons, and the Navy had to terminate the contract against its will. The Navy chose to say the termination was based on a default, rather than acknowledging it was for the government's convenience. In upholding this choice, the Federal Circuit improperly deprived the contractors of the argument that the government's failure to deliver stealth technology was responsible for their performance problems, ignored the contracting officer's opposition to the termination, and changed the governing legal standard from one panel decision to another.

Arguing against review, the government says the contractors cannot complain about the state secrets ruling because they are "plaintiffs." But that is a mere formality. The government was the "moving party" here, carrying the burden of justifying the default. As a result, based on decisions of this Court and other circuits, it was unconscionable for the government to eliminate the contractors' primary

defense while continuing to prosecute the default claim.

The government also argues the Federal Circuit was correct in upholding the default termination based on reasoning flatly inconsistent with the views of the contracting officer at the time. But the rule that the contracting officer must exercise discretion to choose a default termination, and that subsequent review must be limited to the factual bases on which the officer relied, is well established and based on statutory and regulatory requirements as well as principles of fairness reflected in administrative law. Those requirements are particularly important where the government is both decisionmaker and party to a dispute, seeking to effect a forfeiture and inflict other serious penalties.

Finally, the government is simply wrong to deny the circuit split over whether one panel can overrule a prior panel decision in the same case. The 2009 panel expressly recognized that it was changing the law, explaining that the 2003 panel decision was "clearly erroneous" or "manifest[ly] [un]just[]" – by which it apparently meant that the government would have to compensate the contractors for completed work. Pet. App. 27a n.4. Moreover, the government is incorrect that other circuits allow panels to overrule prior panel opinions.

The Federal Circuit's rulings have grave consequences for the contractors, including a government demand for $3 billion. They also have grave implications for all government contractors, for the government's ability to obtain goods and services that are crucial to the Nation's defense, and for the

stability and consistency of the law in a circuit whose docket affects a substantial part of the Nation's economy. This is a case of enormous significance, and this Court's guidance is therefore necessary.

ARGUMENT

1. The government does not dispute the principle, recognized by this Court in *Reynolds* and by the Fourth, Sixth, and D.C. Circuits, that when the government is the "moving party" it may not continue to pursue its case after invoking the state-secrets privilege to deprive the other party of a valid defense. *United States v. Reynolds*, 345 U.S. 1, 12 (1953). The government also does not deny that the default termination was a "government claim," Opp. 14, or that the contractors could have defeated that claim had the state-secrets privilege not barred them from relying on the government's failure to share its stealth technology.[1] The government's sole contention is that because it was formally denominated "defendant" in this case, despite carrying the burden of justifying the default termination, it was entitled to impose a massive forfeiture on the contractors by asserting the virtually unreviewable state-secrets privilege.

But the applicability of the *Reynolds* principle cannot turn on formalistic labels. *Reynolds* speaks of the "moving party," not the "plaintiff." *Reynolds*, 345 U.S. at 12. *Reynolds* was thus concerned not with nominal party designations but with whether the

[1] Given these facts, the contractors plainly do not advocate for a manipulable "[a]utomatic" rule that the government loses its claim once the state-secrets privilege is invoked, regardless of the validity and significance of the affected defense. Opp. 18.

government was pursuing a claim against another party, seeking to use the machinery of justice to enforce or uphold a sanction.

Here, there is no question that the government is the "moving party." It issued a default termination decision that would become *final and enforceable* unless General Dynamics filed an action in court within one year. *See* 41 U.S.C. § 605(b). Once the action was filed, it was the government's burden to justify the default. Therefore, while it is true that General Dynamics filed the first pleading, that was a formality, mandated by statute, which triggered the government's obligation to prove its case. Pet. 16-17.

Although the government argues that this case is "far removed from a criminal prosecution," Opp. 14, courts have repeatedly recognized that default is akin to criminal punishment: it is a "drastic sanction," *J.D. Hedin Constr. Co. v. United States*, 408 F.2d 424, 431 (1969), and a "species of forfeiture," *DeVito v. United States*, 413 F.2d 1147, 1153 (Ct. Cl. 1969), that is the "harshest punishment" the government can visit on a contractor, *Int'l Verbatim Reporters, Inc. v. United States*, 9 Cl. Ct. 710, 716-17 (1986). A defaulted contractor faces not only monetary losses but also substantial disadvantages in seeking future contracts, including potential "debar[ment]." *Malone v. United States*, 849 F.2d 1441, 1145 (Fed. Cir. 1988); *see* FAR 9.406-2(b)(1). In such a situation, the protections of *Reynolds*, and the due process clause, apply just as strongly as if individual liberty were at stake. *Cf. BMW v. Gore*, 517 U.S. 559, 585 (1996)

("that [a party] is a large corporation . . . does not diminish its entitlement" to due process).

It is of no moment that the contractors had to support their affirmative defense of superior knowledge. Opp. 14-15. A defendant *always* bears the burden of proving an affirmative defense – yet the government acknowledges that a claim cannot go forward if a "defendant" is deprived of such a defense by the state-secrets privilege. Indeed, the government has often availed itself of this very rule in civil cases. Pet. 19-21. The governing principle is that the "moving party" in the litigation may not benefit from the invocation of the privilege – and that party here was the government, which retained the ultimate responsibility to justify the default termination. *See Lisbon Contractors, Inc. v. United States*, 828 F.2d 759, 763-65 (Fed. Cir. 1987) ("ultimate burden of proof" on the issue of default remains with the government and never shifts "back and forth"). Put differently, if the parties had presented no evidence after the filing of the pleadings, the contractors would have prevailed.[2]

For all of these reasons, this case is entirely unlike a run-of-the-mill civil action against the government, Opp. 14, or a breach-of-contract action

[2] The government's repeated references to the contractors' superior-knowledge "claim" are therefore inaccurate. Opp. 6, 8-9, 12-19. When (at an early stage) the trial court rejected the government's default claim and converted the termination to one for convenience, the superior-knowledge issue was relevant as one factor in the contractors' quantum of recovery – the scenario to which a number of the government's record citations refer. Opp. 7, 17-18. The only relevant "claim" in the case now, however, is the government's claim for default.

against a private defendant who has terminated a contract, Opp. 15. Such analogies ignore basic government-contracts law. In neither of the government's examples does the defendant hold an administrative judgment against the plaintiff – one that is "final and conclusive" unless the plaintiff brings it to court. 41 U.S.C. § 605(b). Neither of these examples involves a defendant who, once the action is filed, has the duty to move the case forward. Finally, in neither example has the defendant imposed a sanction with serious and ongoing consequences, including non-monetary ones. The "drastic sanction" of a default termination is nothing like a mere refusal to pay money, or a decision simply to terminate a contract. That is precisely why the law unambiguously characterizes *any* attempt to impose a default termination as a government claim, no matter who files the initial pleading. *Lisbon*, 828 F.2d at 764.[3]

Indeed, the fact that the government now demands $3 billion from the contractors – money

[3] For these same reasons, the government's hypothesized government-contracts suit, in which the contractor sues for withheld progress payments but the government never terminates for default, is entirely irrelevant. Opp. 15 n.5. That hypothetical is premised on the *absence* of the very sanction that always – whether or not the government seeks to recover money – amounts to an attack and a punishment. Similarly irrelevant is the government's comparison of this case to one in which an "evidentiary privilege[]" limits access to material. Opp. 16. The contractors here were not deprived of discrete evidence – they were barred from asserting a defense that they could have proved without resort to any privileged material, based merely on the government's unreviewable assertion that the defense would implicate "secret" topics.

that the contractors received for work they performed prior to termination – highlights the absurdity of the government's position that the contractors are the real moving parties here. Attempting to brush this aside, the government insists that the contractors are "highly sophisticated entities that can protect themselves against undue risk." Opp. 19. But this issue is a concern for all government contractors, who are governed by intricate regulations and cannot contract around the risk that the government will continue to pursue a default claim even after using the state-secrets privilege to preempt a key defense. Nor can they turn themselves into defendants, since the government is *always* the nominal defendant in the Court of Federal Claims. All they can do is refuse to enter into contracts involving classified technology.

That prospect has dire implications for the Nation's security. In light of these concerns, and the "unconscionable" result reached by the Federal Circuit, this Court's review is urgently needed.

2. The Federal Circuit's decision also warrants review because it establishes a new standard under which a default termination can be upheld (1) even though the contracting officer did not exercise discretion and (2) based on factual justifications the contracting officer never articulated. Pet. 23-31. The combined effect is that the government can prevail based on a *post hoc* rationalization of a politically motivated decision.

The government does not address whether the contracting officer must exercise discretion, and does not disagree that (as the trial court found) the officer

here was *ordered* to terminate the contract. Pet. App. 97a-98a. Instead, the government contends it is always entitled to prove "that a default termination is justified based on any grounds available, regardless of whether those grounds were known at the time of termination." Opp. 28.

That is incorrect. While the court reviewing a default termination is not bound by a contracting officer's factual *findings*, Opp. 28, it cannot accept factual *bases* for the default wholly different from those on which the contracting officer relied. If it could, there would be no reason for Congress to have specifically required the officer to assess the contractor's performance and state reasons for a termination in writing. Pet. 24-25; 41 U.S.C. § 605(a). There also would be no reason for the separate requirement that the government provide a contractor with an opportunity to cure *before* terminating for failure to "prosecute the work." FAR 52.249-9(a)(1)(ii), (a)(2). The government ignores these requirements – but they have supplied the rule in the Federal Circuit for decades, permitting a court to accept or reject the contracting officer's reasons *de novo*, but forbidding consideration of new reasons invented for litigation.

The cases cited by the government are not to the contrary. As the Petition notes, each involves a situation in which the *post hoc* reason for termination could not have been cured if raised earlier, and was therefore not subject to the cure-notice requirement. Pet. 25-26 & n.6. No such exception applies here, or in any case in which termination rests on an alleged failure to make

progress rather than (for example) a statutory violation, *see Kelso v. Kirk Bros.*, 16 F.3d 1173 (Fed. Cir. 1994), or fraud, *see Joseph Morton Co. v. United States*, 757 F.2d 1273 (Fed. Cir. 1985). Accordingly, if the Federal Circuit's decision stands, the cure-notice requirement and the other statutory and regulatory protections discussed in the Petition will become meaningless formalities. Pet. App. 80a (trial court finding that cure notice "was an item on the checklist," but that "[f]or all practical purposes, the decision to terminate had been made"); *id.* 174a-75a & n.90 (trial court statement that this case established contracting officer's role as "de minimis").

The government's fallback argument is that the question presented is academic because "the rationale on which the officer terminated the contract" was not "different in kind" from the rationale the Federal Circuit used to uphold the termination. Opp. 30. That is simply not true. The contracting officer admitted (and the trial court found) that he and his Navy superiors believed the contractors would fully satisfy the Navy's requirements for the aircraft. *See, e.g.*, Pet. App. 96a n.35, 98a n.40. Consequently, "the reasons [the contracting officer gave] for termination . . . resulted from directions of [the Secretary of Defense's] legal department," *id.* 99a, and reflected no analysis *by anyone* of "the merits" of the "plaintiffs' performance," *id.* 100a.[4] Indeed, the termination

[4] The government quotes after-the-fact trial testimony, Opp. 29-30, but ignores the trial court's ultimate factual findings as well

memo, which the government cites as evidence of "'reasoned judgment,'" Opp. 30, was simply copied wholesale from another Navy program in a last-minute rush, Pet. App. 99a-101a, 411a. And the grounds for default in the cure notice are different from the "alternative theory," Pet. App. 29a, on which the default termination was ultimately sustained.[5]

Under the Federal Circuit's decision, the requirements of a valid cure notice, an informed exercise of discretion involving consideration of specific factors, and a statement of reasons have all been rendered meaningless and no longer impose any check on the government's power to inflict harsh sanctions. That will have devastating and far-reaching effects.

3. This Court's review is also needed to establish a uniform rule regarding when (if ever) one circuit panel may overrule a prior panel in the same case. The government struggles to show that the panel decisions here were consistent, Opp. 22-23 – but the 2009 panel expressly acknowledged that its "current analysis" was "different from the one [it] previously instructed the trial court to perform," Pet. App. 27a n.4. It could hardly have done otherwise, since the 2003 panel required the government to prove that

as evidence of what the contracting officer actually said and did at termination.

[5] The reasons given in the cure notice were failure to "meet specification requirements" and "fabricate parts sufficient to permit final assembly." Opp. 3. The trial court found that both reasons were invalid, and the government never challenged those findings. Pet. App. 55a-56a; *id.* at 79a n.26.

the contractors were failing to progress toward a specific completion date, and the 2009 panel abandoned that requirement. No "intervening" factual developments explain this change in course, Opp. 24, because there were none. Both the 2003 and 2009 panels identified certain facts as relevant, Opp. 23-24, but each thought they were relevant to a different legal question.

The 2009 panel decision therefore gives rise to a clear conflict with other courts of appeals, which bar one panel from overruling another simply because the later panel thinks the earlier one erred. Pet. 33-34. The government tries to paper over the conflict, but primarily relies on cases that have nothing to do with the interaction of appellate panels. *See Arizona v. California*, 460 U.S. 605, 618-19 (1983) (addressing whether this Court is bound by its earlier rulings); *City Pub. Serv. Bd. v. General Elec. Co.*, 935 F.2d 78, 82 (5th Cir. 1991) (considering whether district court correctly barred a claim the court of appeals had held foreclosed); *EEOC v. United Ass'n of Journeymen & Apprentices*, 235 F.3d 244, 249-50 & n.1 (6th Cir. 2000) (addressing whether district court is bound by its earlier rulings); *Johnson v. Champion*, 288 F.3d 1215, 1226 (10th Cir. 2002) (same).[6] It also cites several cases that actually articulate the rule advocated by Petitioner. *See Maxfield v. Cintas Corp.*, 487 F.3d 1132, 1135 (8th Cir. 2007) ("one

[6] Equally inapposite are *Mendenhall v. NTSB*, 213 F.3d 464 (9th Cir. 2000), which was decided ten years *before* the Ninth Circuit case on which Petitioner relies, Pet. 34, and which dealt with a panel lacking statutory authority to act, and *Murphy v. FDIC*, 208 F.3d 959 (11th Cir. 2000), which considered whether a transferor court's rulings bind a transferee court.

panel of this court has no authority to overrule an earlier decision of another panel"); *United States v. Thomas*, 572 F.3d 945, 948 (D.C. Cir. 2009); *cf. United States v. Wallace*, 573 F.3d 82, 89 (1st Cir. 2009) (refusing to overrule earlier panel decision).

In short, the conflict among the circuits is clear. The Federal Circuit's ruling therefore does not, as the government suggests, create merely an "internal difficult[y]." Opp. 25. Rather, it means that litigants in the contractors' position will lose in the Federal Circuit even though they would prevail elsewhere. It also undermines the stability of the law in a circuit where stability is exceedingly important. And it deprives the contractors of *billions* of dollars they would otherwise have received, even though neither the Federal Circuit nor the government has ever identified any actual error or injustice here. This Court should step in to ensure uniformity of the law.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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AMICUS CURIAE BRIEF

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IN THE

Supreme Court of the United States

GENERAL DYNAMICS CORPORATION,
Petitioner,

v.

UNITED STATES,
Respondent.

THE BOEING COMPANY, SUCCESSOR TO
MCDONNELL DOUGLAS CORPORATION,
Petitioner,

v.

UNITED STATES,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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INTEREST OF THE *AMICUS CURIAE*

The Chamber of Commerce of the United States of America (the Chamber) submits this brief as *amicus curiae* in support of the petitions for a writ of certiorari filed by General Dynamics Corporation and The Boeing Company.[1]

The Chamber is the world's largest business federation. The Chamber represents more than 300,000 direct members and indirectly represents an underlying membership of more than three million companies and professional organizations of every size, in every industry sector, and from every region of the country. An important function of the Chamber is to represent the interests of its members in matters before Congress, the Executive Branch, and the courts. To that end, the Chamber regularly files *amicus* briefs in cases that raise issues of vital concern to the nation's business community.

Many members of the Chamber do business with the federal government. The Chamber also represents businesses in industries, such as defense and aerospace, transportation, information technology and telecommunications, which long have served the nation by entering contracts to provide the federal government with goods and services that are vital to national security. Such contracts often relate to

[1] Pursuant to Supreme Court Rule 37.6, *amicus curiae* states that no counsel for any party authored this brief in whole or in part and that no entity or person, aside from *amicus curiae*, its members, and its counsel, made any monetary contribution towards the preparation and submission of this brief. Pursuant to Rule 37.2(a), counsel of record for all parties have received timely notice of *amicus curiae*'s intent to file this brief and have consented to the filing of this brief in letters on file with the Clerk's office.

defense or national security programs that are highly classified, and the contracts themselves may contain classified information. For this reason, one of the questions presented by the petitions for certiorari – whether the Government may maintain a contract claim against a contractor after it asserts the state secrets privilege to deny the contractor a defense to that claim – is of particular concern to the Chamber and its members.

INTRODUCTION AND SUMMARY OF ARGUMENT

This case involves an unprecedented implementation of the state secrets privilege that has far-reaching, adverse effects on the thousands of businesses that contract with the federal government to provide goods and services that are critical to the nation's security. The decision below, by permitting the Government's invocation of the privilege to advance the Government's claim and eliminate a contracting party's defense in a contract dispute, creates considerable uncertainty surrounding the enforceability of government contracts addressing classified matters. That certainty is essential to the effective and efficient delivery of defense systems and services by private companies to the Government, and a decision so severely undermining that certainty presents an important question warranting this Court's review.

In the decisions below, the courts allowed the Government to proceed with its breach of contract claim against Petitioners even though it had asserted the state secrets privilege to deprive Petitioners of the right to litigate a defense to that claim. Pet. App.

202a-203a.[2] The Federal Circuit therefore affirmed a judgment for the Government on the Government's default termination claim – a claim on which the Government is seeking approximately $2.9 billion in contract payments and interest from Petitioners. See General Dynamics Pet. at 11.

That decision – which will effectively govern the litigation of all government contract disputes by virtue of the Federal Circuit's appellate jurisdiction over claims brought in the Court of Federal Claims under the Tucker Act, 28 U.S.C. § 1491, or Contract Disputes Act, 41 U.S.C. §§ 601-613 – warrants this Court's review because it causes great uncertainty and even a deterrent for businesses that enter contracts with the Government in areas such as national security, homeland security, national defense, and intelligence. Such contracts often contain classified information or relate to a government program the operations of which are classified in whole or in part. Under the Federal Circuit's rule, these businesses can no longer be assured that their legal defenses to government contract claims will be judicially enforced if the Government asserts that the evidence relevant to the litigation of the defenses is protected by the state secrets privilege.

Review of the decision below to restore certainty to the contracting process would not call into question the propriety of the Government's invocation of the privilege or the Government's ability to shield from disclosure such privileged information – in this or any other case. Instead, this case concerns what litigation consequences follow from the Government's

[2] Throughout this brief, citations to the Petition Appendix are to the Appendix to the Petition for Writ of Certiorari filed by General Dynamics in No 09-1298.

invocation of the privilege, and it does so only for the important but narrow context of contractual disputes arising between private parties and the Government. For claims brought *against* the Government or contractors by third parties – who have no contractual relationship with the Government, no defense to a contractual claim that could be eliminated upon the Government's invocation of the privilege, no grant of authority to handle classified information, and often no interest in safeguarding the nation's secrets – different litigation consequences are appropriate when the Government invokes the state secrets privilege.

In contrast, the Federal Circuit's decision would disrupt and make less efficient the process that enables the Government to contract to secure goods and services that provide for the nation's security. The Federal Circuit's decision to allow the Government to assert the state secrets privilege and *then* to deprive a contractor of a legal defense to a government contract claim is an unprecedented and unwarranted extension of the privilege that deprives government contractors of the assurance that their contractual rights and defenses will be judicially enforced. The resulting uncertainty threatens to harm businesses that enter contracts with the Government that relate to classified government programs and to undermine their capacity to provide services to the Government. The question presented in the petitions is thus a matter of public importance that warrants this Court's review.[3]

[3] For similar reasons related to the need for certainty in the government contracting process, and because the issues presented by the petitions are intertwined, review of the other issues presented by the petitions is also warranted.

REASONS FOR GRANTING THE PETITIONS

THE FEDERAL CIRCUIT'S UNPRECEDENTED APPLICATION OF THE STATE SECRETS PRIVILEGE UNDERMINES CERTAINTY THAT CONTRACTORS CAN ENFORCE CONTRACTUAL RIGHTS AND ASSERT DEFENSES AGAINST THE GOVERNMENT.

A. The Defense Sector's Ability To Provide Services And Defense Goods To The U.S. Government Depends On Contractual Certainty.

The United States, unlike most other military powers, has chosen to rely upon the innovation and efficiency of the private sector to secure the most sensitive and sophisticated components of its national defense requirements. Other nations have historically relied instead upon agencies and instrumentalities of the government itself (as in the case of former and current Communist governments) or more recently upon companies substantially owned by the government (as in the case of Continental European governments). The United States is able to enlist the resources of private companies only by grounding the defense contracting process in rule of law principles, most importantly by providing certainty that contracts entered with the Government can be enforced.

Since the Revolutionary War, when the Continental Army relied on contractors to provide transportation and engineering services as well as clothing, weapons and labor, the U.S. Government has relied on contractors to provide goods and services to the military. See Moshe Schwartz, Congressional Research Service, *Defense Acquisitions: How DOD Acquires Weapon Systems and Recent Efforts to Reform the Process* 1-2 (July 10, 2009), *available at*

http://www.fas.org/sgp/crs/natsec/RL34026.pdf. Thus, as early as 1775, the Continental Congress established a procurement system and appointed a quartermaster general and a commissary general to buy goods and services for the Continental Army. *Id.* at 2.

Although the threats facing the nation and the needs of the military have changed significantly over the past 235 years, the federal government continues to depend upon the private sector to provide the goods and services necessary to protect the nation. The Department of Defense now relies on thousands of suppliers to provide the weapons, equipment and raw materials to achieve national security objectives, and the defense sector is an important part of the national economy. See Gen. Accounting Office, *DOD Assessments of Supplier-Base Availability for Future Defense Needs; Briefing to the Senate Committee on Banking and Housing, Urban Affairs, Subcommittee on Security and International Trade and Finance* 2 (Oct. 27, 2009), *available at* http:// www.gao.gov/new.items/d10317r.pdf. In 2008, for example, the Department of Defense purchased over $377.5 billion in goods and services from the nation's top 100 defense contractors. Gov't Executive, *Top 100 Defense Contractors* (Aug. 15, 2009), *available at* http://www.govexec.com/story_page.cfm?articleid=43388&printerfriendlyvers=1. And this year, outlays on national defense are estimated to represent almost 20 percent of total federal outlays and almost 5 percent of gross domestic product. U.S. Dep't of Commerce, *Statistical Abstract of the United States: 2010*, tbl.491, at 326, *available at* http://www.census.gov.prod/2009pubs/0statab/defense.pdf.

The U.S. defense contracting process is the principal mechanism that enables the U.S. Government to

secure supplies, including those needed for classified programs, from private corporations in an efficient manner over often lengthy periods. Since the Government first waived sovereign immunity for contract claims in 1855, the assurance that private companies can enforce their contracts against the U.S. Government has been viewed as "indispensable to the efficient operation of government, for without it, qualified private contractors might not undertake government projects ...." Harold J. Krent, *Reconceptualizing Sovereign Immunity*, 45 Vand. L. Rev. 1529, 1565 (1992). This applies equally to contracts involving the most highly classified weapons systems and services and to standard supply contracts. Indeed, defense contracts routinely address classified matters because only the private sector has the capability to develop and produce the most advanced, and thus most classified, technologies in support of the national defense.

Measures that erode the enforceability of defense contracts, as the Federal Circuit's rule does by providing the Government with a discretionary means of avoiding its contractual commitments, undermine the defense sector's ability and willingness to supply the nation's security requirements. For this important sector of our economy to function efficiently, the rules governing the award, administration, and termination of government contracts need to be clearly stated and consistently applied. Cf. *Ducre* v. *Executive Officers of Halter Marine, Inc.*, 752 F.2d 976, 994 n.37 (5th Cir. 1985) (noting the "supremely important interests in predictability and certainty which lie at the heart of contract law"). This adherence to basic "rule of law" principles creates a predictable legal framework that gives businesses the confidence to enter into government

contracts that may extend over several years or contain many contingencies. If, however, the rules become uncertain or tilt toward the Government, the cost of contracting with the Government increases, and some companies may even be unable to enter into contracts with the Government. Increased contractual uncertainty thus threatens not only to undermine the vitality of the economically significant defense sector, but also to increase the cost and lower the range of goods available to the Government. See *United States* v. *Winstar Corp.*, 518 U.S. 839, 913 (1996) (plurality opinion) (Breyer, J., concurring) (if parties are "unwilling to undertake the risk of government contracting," the Government may be unable "to obtain needed goods and services").

B. The State Secrets Privilege, As Applied By The Federal Circuit, Harmfully Undermines Contractual Certainty.

By adding uncertainty to the adjudication of private contractors' defenses to government contract claims, the decision below threatens to harm the many businesses that enter government contracts that contain classified information or relate to classified programs, and harm their ability to provide services efficiently to the Government. Under the Federal Circuit's decision, such businesses can no longer be assured that the judiciary will enforce their defenses to government contract claims. Instead, they face the possibility that, if a contract dispute arises, the Government may assert the state secrets privilege with the effect of preventing the litigation of their contractual defenses.

By reviewing the Federal Circuit's application of the state secrets privilege in this case, the Court could establish a more stable and predictable legal environment and one that ultimately is fair. In the

absence of that review, the importance of the Federal Circuit to shaping the federal contracting process ensures that an unusually high degree of uncertainty is injected into the defense contracting process. The contracting process would shift from one grounded in rule of law principles toward a less workable one more like that governing espionage arrangements, where "contracts" reflect the parties' aspiration and ostensible intent rather than judicially enforceable agreements. See *Tenet* v. *Doe*, 544 U.S. 1 (2005), *Totten* v. *United States*, 92 U.S. 105 (1876). Of course, the party harmed in this situation is the contractor that acted in good faith and, as in these cases, is potentially liable for billions of dollars of liability without an appropriate opportunity to defend against the claim that they breached their contracts.

The source of legal uncertainty is not the Government's ability to invoke the state secrets privilege, but rather the litigation consequences of doing so. Legal certainty can be reestablished without calling into question either the Government's undisputed right to invoke the state secrets privilege if there is a "formal claim of privilege, lodged by the head of the department which has control over the matter," *United States* v. *Reynolds*, 345 U.S. 1, 7-8 (1953), or the Government's absolute right to withhold the information subject to the privilege "if the court is ultimately satisfied that military secrets are at stake." *Id.* at 11. Instead, the issue is whether and in what circumstances the Government can, by invoking the privilege, secure a profoundly unfair advantage in a contractual dispute that it would not otherwise have. The Federal Circuit erred in this limited but crucial respect, and legal certainty would be restored by a determination that the Government's ability to secure that advantage in a contractual

dispute is considerably narrower than what the Federal Circuit's new rule provides. Cf. Pet. App. 202a-210a.

Narrowing the consequences of the Government's invocation of the state secrets privilege in the setting of contract disputes, and particularly in this context, is justified for several reasons. First, the Government is using the state secrets privilege to secure an advantage in the context of a contract it has already entered. The Federal Circuit's rule permits the Government to assert a claim under the contract while retaining the discretion to invoke the privilege to avoid a defense to the claim. This result is horribly one-sided and has the detrimental effects outlined above. See *supra* pp. 7-8. Second, the Government is invoking the privilege in a context where the private parties to the contract have the ability and incentive to safeguard classified information. Defense contractors on a daily basis handle many of the nation's most sensitive secrets and must agree not to disclose such information. See Info. Security Oversight Office, *Classified Information Nondisclosure Agreement Briefing Booklet* (discussing the nondisclosure agreement that must be signed by employees of government contractors and consequences related to breach), *available at* http://www.archives.gov/isoo/training/standard-form-312.html ("Briefing Booklet"). Indeed, the contract at issue in this case directly addressed classified information that was presumably very closely related to the classified information subject to the state secrets doctrine. See Pet. App. 245 (state secrets doctrine applying to information the Court of Federal Claims found to be necessary to litigate Petitioners' "superior

knowledge" defense).[4] Sanctions associated with contractors' disclosure of classified information are severe. See Briefing Booklet, *supra*, at Question 20 (the Government "may move to terminate the contract or to seek monetary damages from the contractor, based on the terms of the contract" and may also criminally prosecute individuals or organizations). Finally, as discussed below, permitting the Government to invoke the privilege to assist it purely in litigating a contractual claim it asserts against a private party is contrary to established equitable principles and judicial processes. See *infra* pp. 13-16.

Review in this case would thus not call into question the broader effects on litigation appropriately produced when the Government invokes the state secrets privilege in cases brought by third parties against the Government or its contractors. See, *e.g.*, *Mohamed* v. *Jeppesen Dataplan, Inc.*, 579 F.3d 943 (9th Cir.), *reh'g en banc granted*, 586 F.3d 1108 (9th Cir. 2009); *El-Masri* v. *United States*, 479 F.3d 296 (4th Cir. 2007); *Al-Haramain Islamic Found., Inc.* v. *Bush*, 507 F.3d 1190 (9th Cir. 2007); *Hepting* v. *AT&T Corp.*, 439 F. Supp. 2d 974 (N.D. Cal. 2006).[5] There, the plaintiffs have no contract

[4] The Chamber does not dispute the Government's assertion that the stealth aircraft technology at issue in this case is protected by the privilege, and its knowledge of the facts of this case is limited to those set forth in the lower court opinions reprinted in the Petition Appendices, which of course are public materials.

[5] The Chamber filed an *amicus* brief in support of the Government's assertion that the state secrets privilege required dismissal of a third party's claim against a company alleged to have contracted with the Government regarding matters relating to national security. *See* Brief of *Amicus Curiae* Chamber of Commerce of the United States of America in Support of Appellants and Urging Reversal in *Hepting* v. *AT&T*

with the Government, have not been selected by the Government for their ability to handle classified information, and by definition bring claims *against* the Government – often in the form of advocacy litigation designed to increase the disclosure and scrutiny of sensitive national security information.

C. The Government's Ability To Use The State Secrets Privilege To Further Its Claims Against Defense Contractors Especially Undermines Contractual Certainty.

Certainty surrounding defense suppliers' contracts and particularly the remedies available when a dispute arises between the parties is especially undermined if the Government can use the state secrets privilege not only to withhold information, but also to deprive a private contracting party of a defense against the Government's own contractual claim. The Federal Circuit's rule operates in just this manner. In this case, the Government is acting as the "moving party" on the default termination claim. *United States* v. *Reynolds*, 345 U.S. at 12 (state secret invocation providing litigation benefit to the Government upheld because the Government is not the "moving party"). The Government bore the burden of proving that Petitioners were in default of their contractual obligations (Pet. App. 196a-197a), and it sought the repayment of billions of dollars from Petitioners after it prevailed on this claim in the courts below. General Dynamics Pet. at 11. As a result of the Government's assertion of the state secrets privilege, as applied by the Federal Circuit,

Corp., 539 F.3d 1157 (9th Cir. 2008). The Chamber's submission in this case is completely consistent with its position in *Hepting*.

Petitioners were stripped of their defense to this claim.

In criminal and civil contexts, a government generally cannot both assert a privilege and, as a result, secure a litigation advantage for its own claim. For example, a government cannot pursue a claim and assert foreign sovereign immunity as a defense to counterclaims. See 28 U.S.C. § 1607; *Cabiri* v. *Gov't of Ghana*, 165 F.3d 193 (2d Cir. 1999). Nor can a state government pursue a claim and advance that claim, or deflect counterclaims, by invoking state sovereign immunity recognized by the Eleventh Amendment. See, *e.g.*, *Lapides* v. *Bd. of Regents*, 535 U.S. 613, 619 (2002) (State waives Eleventh Amendment immunity by removing case to federal court; allowing States "to follow their litigation interests by freely asserting both [a claim and immunity] in the same case could generate seriously unfair results"); *Gardner* v. *New Jersey*, 329 U.S. 565, 574 (1947) (when State files a bankruptcy claim, "it waives any immunity which it otherwise might have had respecting the adjudication of the claim").

This principle should extend equally to the Government's privileges related to classified information and the nation's security. For example, the Classified Information Procedures Act ("CIPA") is designed to provide a measure of protection to the Government's use of classified information in the course of prosecutions. See 18 U.S.C. app. 3 §§ 1-16. The Government may not, however, use CIPA's provisions to secure a material litigation advantage; the Government is required instead to abandon the claim relevant to the information the Government chooses not to disclose. See *id.* § 6(e)(2) (dismissal of claim or count, or finding against Government); see also *id.* § 12(b). In addition, outside the context of CIPA, the

Government must choose between pursuing a prosecution and invoking executive privilege to protect classified information or other government secrets material to a defense against the Government's case. See *United States* v. *Smith*, 780 F.2d 1102, 1107-08 (4th Cir. 1985) (en banc); see also *Roviaro* v. *United States*, 353 U.S. 53, 60 (1957).

The Federal Circuit's decision to allow the Government to proceed on this default termination claim while simultaneously invoking the state secrets privilege to deprive Petitioners of a defense to the claim is, moreover, more broadly inconsistent with the courts' general refusal to allow any litigants to use a privilege as both a sword and a shield. See, *e.g.*, *United States* v. *Rylander*, 460 U.S. 752, 761 (1983) (Fifth Amendment privilege against self-incrimination); *Bittaker* v. *Woodford*, 331 F.3d 715 (9th Cir. 2003) (attorney-client privilege); *Wehling* v. *CBS*, 608 F.2d 1084, 1087 (5th Cir. 1980) (Fifth Amendment privilege against self-incrimination). These decisions are based on the recognition that it is fundamentally unfair to permit a litigant to proceed with a claim while declining to provide the other party with the information needed to prepare a defense to the claim. See, *e.g.*, *Wehling*, 608 F.2d at 1087; cf. *Lindsey* v. *Normet*, 405 U.S. 56, 66 (1972) ("Due process requires that there be an opportunity to present every available defense") (internal quotation marks omitted).

This Court's leading state secret doctrine decision similarly indicates that there are limits on the Government's ability to assert the state secrets privilege and secure a litigation benefit for its own claim, although the Court had no occasion to address the issue directly or to define the full implications of the invocation of the doctrine for the Government's

own claim. *United States* v. *Reynolds*, 345 U.S. 1, involved a tort suit brought against the United States by three widows whose husbands were killed when an Air Force plane crashed during a flight to test secret electronic equipment. *Id.* at 3. This Court upheld the invocation of the privilege even though it deprived plaintiffs of evidence they sought in pursuit of their claims. The Court distinguished criminal cases where the Government "can invoke its evidentiary privileges only at the price of letting the defendant go free," *id.* at 12, on the basis that the case arose "in a civil forum where the Government is not the moving party, but is a defendant only on terms to which it has consented." *Id.*

This case thus also provides the opportunity for this Court to elaborate the point it raised in *Reynolds*, and to resolve the important question whether, when the Government seeks to pursue a claim in a civil action after asserting the state secrets privilege, the court must also apply the privilege to deprive the other party of a defense to that claim. What makes the Government's claim particularly unfair is that the Government does not lose the ability to terminate a contract if state secrets are implicated in the parties' dispute and the standard means of protecting classified information short of invocation of the state secrets privilege are insufficient. Instead, the Government is limited to the remedies of a termination for convenience, which are substantial, but not one-sided. See, *e.g.*, Krent, *supra*, at 1565-66 (when the Government terminates a contract for convenience, it may "escape the full consequences of a breach" because the contractor may not obtain specific performance and its recovery is generally limited to costs incurred, profit on work done, and the cost of preparing the termination settlement pro-

posal). Thus, the interests of the Government can be fully protected without having to impose undue burdens on contractors and thereby create disincentives for future potential contractors to undertake to promote the Government's most sensitive and important national security and defense assignments.

In light of the far-reaching and unfair effects of the Federal Circuit's decision below, the question whether the Government may use the state secrets doctrine not only as a shield to prevent the disclosure of privileged information, but also as a sword to strike a contractor's defense to the Government's own contract claim, presents an important question that merits this Court's review.

CONCLUSION

For the foregoing reasons, the petitions for a writ of certiorari should be granted.

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AMICUS CURIAE BRIEF

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In the
Supreme Court of the United States

♦

GENERAL DYNAMICS CORPORATION, PETITIONER,

v.

UNITED STATES OF AMERICA

♦

THE BOEING COMPANY, PETITIONER,

v.

UNITED STATES OF AMERICA

♦

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

♦

BRIEF OF NATIONAL DEFENSE INDUSTRIAL ASSOCIATION AS AMICUS CURIAE SUPPORTING PETITIONERS

♦

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The National Defense Industrial Association ("NDIA") respectfully submits this brief as amicus curiae in support of petitioners.[1]

INTEREST OF AMICUS CURIAE

The NDIA is a nonpartisan, nonprofit organization with a membership that includes over 1,700 companies and 80,000 individuals. NDIA's members provide a wide variety of goods and services to the government and include some of the Nation's largest defense and homeland security contractors. Among other things, NDIA's members perform, and may be asked in the future to perform, large-scale research and development contracts with the government similar to the one awarded to petitioners to design, manufacture, and test the "A-12 Avenger" aircraft.

The issues in this case are of substantial interest to NDIA's members, because they affect the circumstances under which the government can terminate fixed-price research and development contracts, and

[1] Pursuant to Rule 37.2(a), the parties' counsel of record were notified ten days prior to the due date of the intention to file this brief. Copies of letters consenting to the filing of this brief by the parties have been filed with the Clerk of the Court. No counsel for a party authored this brief in whole or in part, and no party or counsel for a party made a monetary contribution intended to fund the preparation or submission of the brief. No person other than amicus curiae, its members, or its counsel made a monetary contribution to the preparation or submission of this brief.

the manner in which the government can subsequently justify its terminations in court. The ruling below, if not reversed by this Court, exposes NDIA members to the severe consequences of default termination, based not on contract performance but on waning political or economic support. Such results create significant risks that will severely undermine NDIA's members' abilities and incentives to undertake future government contracts.

SUMMARY OF ARGUMENT

The government possesses extraordinary power to terminate its own contractual obligations. The Federal Acquisition Regulation, which governs every federal procurement contract, allows the government to terminate a contract at any time, for almost any reason, for its own convenience. 48 C.F.R. § 49.101(a). There are virtually no consequences to the government for a termination for convenience. The government simply walks away from the deal and must only reimburse the contractor for costs reasonably incurred and (in some cases) a reasonable profit on those costs. *Maxima Corp. v. United States*, 847 F.2d 1549, 1552 (Fed. Cir. 1988).

The government also can, under circumstances broadly expanded by the ruling below, terminate a contract for "default." 48 C.F.R. § 49.101(a). The consequences to the contractor for a default termination are severe. *DeVito v. United States*, 413 F.2d 1147, 1153 (Ct. Cl. 1969). The contractor is denied payment for out-of-pocket costs that have not already been reimbursed, and the contractor may be required to pay back all progress payments it has received for work that has not yet been accepted by the government. 48 C.F.R. § 49.402-2(a). A default termination also can result in the contractor being barred from public contracting, or being prejudiced in the award of new contracts. *Id.* § 9.406-2(b)(1).

After the fact, contractors can contest a default termination and require the government to *prove* the

grounds for default. But even if the contractor ultimately prevails in the litigation due to the government's failure to justify its default termination, the termination is simply converted into one for convenience, as the government is not subjected to ordinary breach damages. *Darwin Constr. Co. v. United States*, 811 F.2d 593, 597 (Fed. Cir. 1987).

A. The Federal Circuit's multi-billion dollar forfeiture in this case effects an unprecedented expansion of the government's ability to terminate a government contract for default. This Court's review is imperative because the ruling below strips from contractors significant procedural protections and alters the substantive requirements of what the government must prove to sustain a default termination.

1. Until the ruling below, longstanding precedent had required that the contracting officer decide and articulate the basis for a default termination after considering several specific factors enumerated in the Federal Acquisition Regulation. Such procedures guaranteed that the government official with the authority and knowledge to administer the contract was the person actually assessing the contractor's performance.

But the ruling below, rather than requiring the government to rely on the grounds actually given by the contracting officer in cancelling the contract, allows the government to concoct an after-the-fact rationale to justify the default termination. The government's termination can now be sustained so long

as there is some "nexus" between the decision to terminate and the contractor's performance. The Court should review this departure from prior government contracting principles, because it relieves the contracting officer of the burden of justifying a default termination and places that responsibility in the hands of government litigators, who are free to create an after-the-fact analysis and justification.

2. Moreover, in addition to removing significant procedural protections on which contractors have long relied, the ruling below eliminates an important objective standard under which the government's justification for default terminations had been measured.

Before the Federal Circuit's ruling, a fixed-price contract could be terminated for default when "there was no reasonable likelihood that the contractor could perform the entire contract effort within the time remaining for contract performance." *Lisbon Contractors, Inc. v. United States*, 828 F.2d 759, 765 (Fed. Cir. 1987) (citation and brackets omitted). But where the government is unable to meet that standard because the government has previously excused the contract completion date during contract performance the Federal Circuit's decision permits a contract to be terminated for default whenever the government "feel[s] insecure about the contractors' rate of progress." This low threshold for default termination ignores the reality of massive fixed-priced research and development contracts, which sometimes require significant flexibility as the contractor attempts an undertaking that has never been

accomplished. If left standing, the ruling below will discourage contractors from entering such innovation-generating contracts.

B. The Federal Circuit's ruling, which permits the government to pursue a claim against contractors and then to invoke the state-secrets privilege to deprive them of a valid defense to that claim, provides an independent basis for this Court's review. The decision cannot be reconciled with decisions of this Court or those of several courts of appeals.

The state-secrets holding in this case will have a profound effect on government contractors, including NDIA's members. Many government contracts require the contractor either to use or to develop classified material. The mere existence of this top-secret information now provides the government with a potential basis to invoke the privilege whenever the contractor seeks to raise a valid defense to a government claim of default.

C. The Federal Circuit's decision will have catastrophic effects on the government-contracting industry. The Department of Defense invests hundreds of billions of dollars in government contracts and relies on those contracts to provide a wide array of services. The uncertainty and fundamental unfairness resulting from the unbridled authority bestowed on the government by the Federal Circuit's decision, however, either will discourage contractors from engaging in particularly risky or difficult-to-achieve contracts with the government or will cause

such engagements to become more costly to taxpayers.

More specifically, and more importantly, the Federal Circuit's decision will discourage major research and development projects. These projects are the foundation of significant advances to our Nation's defense, yet they often require flexibility as contractors are asked to work in uncharted territory. It is commonplace for these contracts to experience cost and schedule overruns, which the government often waives based on its own recognition that the contract goal was not attainable in the time or under the terms originally contemplated. That such a common reality could now be the basis for a default termination particularly where the government has *waived* the contract completion date will discourage contractors from entering into these contracts in the future.

ARGUMENT

REVIEW IS NECESSARY BECAUSE THE FEDERAL CIRCUIT'S DECISION CREATES SIGNIFICANT UNCERTAINTY REGARDING THE PRINCIPLES THAT CONTROL THE GOVERNMENT'S TERMINATION OF ITS CONTRACTS WITH THE NATION'S CONTRACTORS

A. The Federal Circuit's Ruling Confers Virtually Unconstrained Power On The Government Arbitrarily To Terminate Contracts For Default

Under the ruling below, the contracting officer has the power to terminate a government contract for default without any evaluation of the contractor's actual performance. Worse still, the Federal Circuit held that judicial review of the contracting officer's termination decision need not be confined to the contemporaneous justification. This result eliminates the previously clear standards on which NDIA's members have long relied when investing billions of dollars to complete contracts, substituting a regime in which a default termination can be upheld on any ground even post hoc grounds never considered or articulated by the contracting officer when making the actual termination decision. This result conflicts with the plain language of the Contract Disputes Act and nearly a century of judicial precedent. Review by this Court is warranted.

1. a. This Court should review the Federal Circuit's ruling because it upsets settled rules that

govern most government contracts. Like petitioners, many of NDIA's members and other contractors have long relied on previously settled procedural principles when entering contracts with the government. While contractors must assume the risk of a termination for convenience that is, the risk that the government may choose to walk away from its contractual obligations for virtually any reason without incurring ordinary contract breach damages contractors have been protected (at least until the ruling below) by the requirement that the government must articulate a sound, rather than pretextual, basis for a default termination.

Before this case, the explicit factors enumerated in the Federal Acquisition Regulation (discussed below) have guided NDIA's members in assessing risks before entering into particular contracts and have minimized the risk of termination during performance. These are particularly important considerations because, unlike a termination for convenience, a default termination is "a species of forfeiture," *DeVito*, 413 F.2d at 1153, with "the most serious consequences for a contractor," *Appeal of Executive Elevator Serv.*, No. VABCA-2152, 1987 VA BCA Lexis 81, at *44 (May 15, 1987).

b. The Contract Disputes Act provides that "[a]ll claims by the government against a contractor relating to a contract shall be the subject of a decision by the contracting officer." 41 U.S.C. § 605(a). Any decsion by the contracting officer must be reasoned and capable of judicial review: "The contracting

officer shall issue his decision in writing [and] * * * shall state the reasons for the decision reached * * * ." *Ibid.* Moreover, far from conferring unbridled discretion on the contracting officer, a default determination *requires* that the contracting officer "shall consider" several enumerated factors before deciding that the contractor cannot complete the contract within the allotted time frame. 48 C.F.R. § 49.402-3(f). These factors include "[t]he terms of the contract" and "the specific failure of the contractor and the excuses for the failure." *Ibid.* These provisions guarantee that the contracting officer the government official with the actual authority and knowledge to administer the contract and the person who interacts with the contractors on a regular basis—is the decisionmaker to judge the contractor's performance.

Consistent with these principles, courts have long held that the government must be held "strict[ly] accountab[le]" for its decision to terminate a contract for default. *H.N. Bailey & Assoc. v. United States*, 196 Ct. Cl. 156, 163 (1971). To that end, the government must dedicate "genuine consideration" to the relevant information rather "than a *pro forma* check off of" the factors. *Appeal of JAMCO Constructors, Inc.*, No. VABCA-3271, 1993 VA BCA Lexis 30, at *54 (Oct. 5, 1993). The Federal Circuit's predecessor court long held that this is a "protective rule" that ensures the government contractor is being treated fairly. *Schlesinger v. United States*, 390 F.2d 702, 709 (Ct. Cl. 1968). And it ensures that the

government has some basis for terminating a contract for default. *Acme Process Equip. Co. v. United States*, 347 F.2d 509, 528 (Ct. Cl. 1965) (explaining that the government "may always sever contractual relations" for convenience, but if it "seeks instead to annul a contract for fault, thereby leaving the contractor wholly uncompensated, it must have proper justification for such harsh consequences"), rev'd on other grounds, 385 U.S. 138 (1966).

c. There can be no dispute that *none* of this actually occurred in this case, and, absent this Court's review, there now can be *no* assurance that it ever will occur in the future. Here, the trial court found that the contracting officer did not exercise his own discretion in applying the regulatory factors relating to default terminations but acted because *political* support for the contract was waning and then-Secretary of Defense Cheney ordered that the contract be terminated. General Dynamics Pet. App. ("GD App.") 411a; Boeing Pet. App. ("Boeing App.") 442a. ("In the end, the contract was not terminated because of contractor default. It was terminated because the Office of the Secretary of Defense withdrew support and funding."). Indeed, as the trial court explained:

> The contracting officer's use of contractor default was based on his general familiarity with the contractors' performance, which previously he had not believed justified a default termination. He did not consult with technical personnel. He did not review the

> contractors' claims for equitable adjustments. He did not give adequate attention to the claims that may have excused the alleged default in that time, especially those involving superior knowledge issues.

GD App. 411a; Boeing App. 442a. Thus, the contracting officer's termination "memorandum was cribbed" from a memorandum related to "another program," GD App. 411a; Boeing App. 443a, and plainly demonstrated "that consideration of the [Federal Acquisition Regulation] factors was non existent. The entire termination procedure was *pro forma* at best." GD App. 412a; Boeing App. 443a-444a.

Although the default termination could not be sustained under previously established law, the Federal Circuit in this case adopted a new standard to review such determinations: "there must be a nexus between the government's decision to terminate for default and the contractor's performance." GD App. 269a; Boeing App. 95a. This "nexus" requirement is satisfied so long as "the termination for default was predicated on contract related issues." GD App. 251a; Boeing App. 75a. And it permits a default termination without requiring the government "to establish that the contracting officer conducted the analysis necessary to sustain a default under the alternative theory." GD App. 29a; Boeing App. 31a.[2] In other

[2] Although the court below later relied on two decisions for this proposition—*Empire Energy Mgmt. Sys. v. Roche*, 362 F.3d 1343, 1357 (Fed. Cir. 2004), and *Christopher Vill., L.P. v. United*

(Continued on following page)

words, the Federal Circuit's standard relieves the contracting officer of any burden to analyze or to articulate a basis for a default termination, and instead places that responsibility in the hands of government litigators, who are free to adopt an after-the-fact analysis and justification.

2. Perhaps even more troubling, the Federal Circuit's ruling also exposes NDIA's members to the consequences of a default termination whenever the government's litigators can subsequently prove that a contracting officer might have felt "insecure about the contractors' rate of progress" when there is no valid contract completion date. GD App. 27a; Boeing App. 29a. Thus, the Federal Circuit's ruling both permits the government to justify its decision after the fact and without regard to what the contracting officer actually believed *and* it eliminates a meaningful objective standard by which to measure the contractor's nonperformance in assessing a default termination.

a. The Court should review the ruling below because, in contracts without a valid contract completion date, the government can wait and see how the project continues to progress, without establishing a

States, 360 F.3d 1319, 1337 (Fed. Cir. 2004)—both were decided *after* the court's earlier opinion in this case articulated its new standard. If anything, the court's reliance on those cases demonstrates that the Federal Circuit has abandoned, and without this Court's review will continue to abandon, the requirements of the Contract Disputes Act and the Federal Acquisition Regulation.

new completion date, in order to take advantage of the Federal Circuit's more lenient ad hoc default termination standard. If the ruling is not reversed, contractors will have less incentive to enter costly, fixed-priced research and development projects where completion of the contract might require the contractor and the government to revise specifications and the contract's schedule, because that needed flexibility subsequently may be used *against* the contractor when the government seeks to terminate a contract for default. Moreover, contractors will be prejudiced by the fact that they must continue to invest significant money into research and development—in this case between $120 to $150 million per month, GD App. 6a; Boeing App. 7a without knowing whether time is "of the essence" and that there is a possibility of termination for default. *DeVito*, 413 F.2d at 1154.

b. Once again, the Federal Circuit's decision cannot be reconciled with government contract principles on which petitioners and NDIA's members have long relied. Under fixed-price research and development contracts like the one at issue here, the government is permitted to terminate a contract for default when a contractor "fails to * * * [p]rosecute the work so as to endanger performance of" the contract. 48 C.F.R. § 52.249-9(a)(1)(ii). Under previously governing precedent, a default termination on this ground could be justified only when there was "no reasonable likelihood that the contractor could perform the entire contract effort within the time

remaining for contract performance." *Lisbon*, 828 F.2d at 765 (citation and brackets omitted). Accordingly, the government could not terminate a contract for default merely because the contractor fell behind schedule.

These principles are particularly vital to massive, fixed-price research and development contracts on which this Nation depends for cutting-edge technology. Significant flexibility is often required indeed, assumed in research and development contracts, so that the contractors and the government can meet their stated goal, which is often one that has never been accomplished. *See* 48 C.F.R. § 35.002 (noting that research and development contracts "are directed toward objectives for which the work or methods cannot be precisely described in advance" and that the contracting process should be adapted to provide "reasonable flexibility and minimum administrative burden"). Thus, sometimes technical specifications, interim deadlines, or the contract completion date, which might have seemed attainable at the outset, are later deemed unrealistic and are excused by the government. GAO, Report No. 09-326SP, *Defense Acquisitions: Assessments of Selected Weapon Programs* 6, 9-11 (Mar. 2009). NDIA's members have found that both contractors and the government need this flexibility to modify these requirements and milestones as such projects progress and unexpected hurdles must be overcome. And in the process, it is not unheard of (as occurred here, GD App. 71a-72a; Boeing App. 145a-146a) for the contract completion

date after being waived by the government to remain undefined for some period of time as research and development progresses.

* * *

The ruling below effects a sea change in government contract law. It fundamentally changes the procedures for termination by effectively eliminating the important safeguard that the contracting officer must exercise reasoned discretion in any termination decision. And it eliminates, in contracts where the government has excused the contract completion date, the objective requirement that a default termination can be sustained only when there is "no reasonable likelihood that the contractor could perform the entire contract effort within the time remaining for contract performance." *Lisbon*, 828 F.2d at 765 (citation and brackets omitted). Because the Federal Circuit's ruling below will govern almost every government contract dispute, 28 U.S.C. § 1295(a)(3), (10), review is warranted.

B. The Government's Invocation Of The State-Secrets Privilege To Preclude A Contractor's Defense Cannot Be Reconciled With This Court's Precedent Or That Of Other Courts Of Appeals

Equally egregious, and an independent basis for this Court's review, is the Federal Circuit's ruling that the government could invoke the state-secrets privilege to defeat the contractors' superior knowledge defense. That ruling allows the government to

pursue a forfeiture claim (here a multi-billion dollar claim) against private parties, such as NDIA's members, while at the same time the government deprives those parties of a valid defense in this case, one that does not even require the contractors to use state secrets. The Federal Circuit's ruling is unprecedented and, if left standing, will adversely affect the Nation's most sensitive government contracting.

a. As both petitions demonstrate (GD Pet. 13-21; Boeing Pet. 18-23), the Federal Circuit's decision conflicts with decisions of this Court and those of several courts of appeals.

Over half a century ago, in *United States v. Reynolds*, this Court held that the government could refuse, by invoking the state-secrets privilege, to produce certain documents sought by a private plaintiff in a Federal Tort Claims Act suit. 345 U.S. 1, 6-7 (1953). But in upholding that invocation, the Court made a point of observing that "the Government [wa]s not the moving party" in the litigation. *Id.* at 12. The Court thus distinguished the situation there from the "unconscionable" situation in which the government *pursues* a claim "and then invoke[s] its governmental privileges to deprive the accused of anything which might be material to his defense." *Ibid.* As a moving party, this Court observed, the government "can invoke its evidentiary privileges only at the price of" relinquishing its claim. *Ibid.*

Although the situation in which the government is pressing the claim most often arises in the criminal

context, the principle on which the Court's observation in *Reynolds* is based should not depend on the type of case, but rather on whether the government is "the moving party." Thus, this Court has recognized that the government must relinquish its claim against an accused if the government withholds documents, even due to "vital national interests," that are necessary for the accused's defense. *Jencks v. United States*, 353 U.S. 657, 670 (1957); *see also Roviaro v. United States*, 353 U.S. 53, 60-61 (1957) (recognizing that governmental privileges "must give way" where the disclosure "is relevant and helpful to the defense of an accused").[3]

b. The Federal Circuit's decision also conflicts with decisions of the D.C., Fourth, and Sixth Circuits. Those courts, following *Reynolds*, have consistently precluded civil claims from going forward when a defendant's valid defense to those claims would require the disclosure of state secrets.

The D.C. Circuit has explained that, "when the district court can determine that the defendant will be deprived of a valid defense based on the privileged

[3] The Federal Circuit held that dismissal was not required here because this was a civil, rather than a criminal, case. GD App. 209a; Boeing App. 70a-71a. But, as discussed above, *Reynolds* should not be read so narrowly. Moreover, as Boeing explains (Boeing Pet. 31-32), the penalty imposed in this case a form of forfeiture is closely related to a criminal sanction, and there is no basis under this Court's precedent to deprive even civil litigants of every available defense.

materials, it may properly dismiss the complaint." *In re Sealed Cases*, 494 F.3d 139, 149 (D.C. Cir. 2007). Thus, in a civil case against the government where invocation of the state-secrets privilege prevented the government from asserting a valid defense, the D.C. Circuit held that dismissal of the case would be appropriate. *Id.* at 151; *see also Molerio v. FBI*, 749 F.2d 815, 825 (D.C. Cir. 1984) (Scalia, J.) (affirming dismissal because evidence protected by the state-secrets privilege precluded the government from presenting a defense).

The Fourth Circuit similarly has held that dismissal is proper where "the defendants could not properly defend themselves without using privileged evidence." *El-Masri v. United States*, 479 F.3d 296, 309 (4th Cir. 2007). Thus, where invocation of the state-secrets privilege precluded a defense to a claim of civil liability, the court of appeals held that the plaintiff's case could not proceed.

Likewise, the Sixth Circuit held that "[b]ecause the state secrets doctrine thus deprives [d]efendants of a valid defense to [plaintiffs'] claims, we find that the district court properly dismissed the claims." *Tenenbaum v. Simonini*, 372 F.3d 776, 777 (6th Cir. 2004). There, plaintiffs had sued the government and various federal agency employees, and the government moved for summary judgment because it could not assert a defense without the disclosure of information protected by the state-secrets privilege. *Ibid.*

Courts also have recognized that a plaintiff's claims must be rejected if the government's invocation of the state-secrets privilege precludes the plaintiff from mounting a prima facie case of liability. *See, e.g.*, *Kasza v. Browner*, 133 F.3d 1159, 1166 (9th Cir. 1998); *Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1142-1143 (5th Cir. 1992); *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 547 (2d Cir. 1991). But no authority, other than the Federal Circuit's ruling below, permits the government to assert its own affirmative claim and then use the state-secrets privilege to deprive the defendant of a valid defense to that government claim. Indeed, the fundamental unfairness of the ruling below (and the need for this Court's review) is made plain by the simple fact that the government readily insists on (and obtains) dismissal of claims against it when its own invocation of the privilege deprives it of a defense.

c. While this conflict alone makes the Federal Circuit's ruling worthy of review, that the state-secrets privilege will now be applied to government contracts makes review imperative.

Many government contracts, and particularly those in the defense industry where amicus NDIA's members have expertise, require contractors to use and develop classified technology. In many contracts, the mere existence of this classified information would provide the government with a potential basis to invoke the state-secrets privilege whenever the

contractor seeks to raise a valid defense to a government claim of default.

Accordingly, if left standing, the Federal Circuit's ruling will place NDIA's members in a fundamentally untenable and unfair situation with respect to many of their contracts: if the government were to terminate those contracts on an allegation of default, the government could preclude the contractor from raising valid defenses while still subjecting the contractor to the government's forfeiture claim. This troubling result is unnecessary, as the government suffers very little prejudice if its invocation of the privilege results in its inability to press its default-termination claim. In that event, the government would not be subjected to ordinary contract breach damages. Rather, the termination would simply be transformed into one for convenience which is hardly the equivalent of letting a potential criminal go free, a result that is accepted when the government invokes the state-secrets privilege against someone it criminally has accused. *See, e.g.*, *Jencks*, 353 U.S. at 671-672. Moreover, where the government decides it needs to invoke its state-secrets privilege to prevent a contractor from defending against the government's forfeiture claim, a termination for convenience of the government is the appropriate result.

Indeed, this Court's review is particularly needed because the ruling below provides an incentive to the government to assert the privilege, without regard to any necessity to do so. Because courts defer to the

government when reviewing an invocation of the state-secrets privilege (lest that scrutiny result in the disclosure of the very information the privilege is designed to protect), the government's assertion of the privilege is almost never successfully contested (if it is even contested at all). *See, e.g., El-Masri*, 479 F.3d at 305-306. Indeed, as this Court has explained, the propriety of the invocation often is immune even from *in camera* review. *Reynolds*, 345 U.S. at 10. Thus, the government has every opportunity and motive to assert the privilege, even where it might be unnecessary or inappropriate to do so.

In fact, *Reynolds* itself provides a potential example of just such a case. Fifty years after that decision, access to previously classified reports raise serious questions as to the legitimacy, or at least the necessity, of the government's privilege claim. *See Herring v. United States*, No. 03-cv-5500, 2004 WL 2040272 (E.D. Pa. Sept. 10, 2004), aff'd, 424 F.3d 384 (3d Cir. 2005). While NDIA and its members do not dispute that cases exist in which certain closely-guarded information must be kept confidential, the government's decision to invoke the privilege should not come at the expense of contractors who are merely trying to present a valid defense to a government forfeiture claim. GD App. 245a; Boeing App. 294a (noting that the contractors "made a persuasive showing that they could prove" the superior-knowledge defense without the need for any top-secret information).

C. The Ruling Below Will Hinder The Nation's Ability To Develop Cutting-Edge Defense Technology

As discussed above, the Federal Circuit's decision significantly undermines settled expectations that undergird billions of dollars' worth of contracts with the government

1. As NDIA's members can attest, the relationship between our government and its contractors depends on stability in the law and, because the government possesses the unique power to terminate contracts, principles of trust and fairness. Just as the government invests significant taxpayer resources into contracts with its contractors, these contractors which include many of the Nation's most important businesses invest billions of dollars of their own funds into research and development to meet contractual obligations. But the uncertainty and fundamental unfairness that results from the Federal Circuit's decision will discourage contractors from engaging in risky or difficult-to-achieve contracts with the government. At a minimum, the Federal Circuit's ruling, if left standing, will cause such engagements to become more costly to taxpayers, as businesses must account for an increased and unpredictable possibility that the government might terminate a contract for default even when the termination is motivated by politics or cost, rather than by contractor fault.

This unbridled authority granted to the government by the Federal Circuit places at risk current government contracts worth hundreds of billions of dollars and will deter contractors from entertaining certain high-risk contracts with the government in the future. Under the Federal Circuit's ruling, NDIA's members and other contractors no longer will be capable of preventing or anticipating when they may be found in default, as even assurances from those within the government with whom the contractor may be working including the contracting officer—are insufficient to insulate a high-priced or unpopular contract from political default termination. GD App. 410a-411a; Boeing App. 441a-442a. Indeed, in another case, after recognizing that "the dollars at stake" were "so large" that they caused the government to act in an unjust way, the Chief Judge of the U.S. Court of Federal Claims noted that "one is almost tempted to wonder if insanity is indeed a prerequisite for contracting with the Government." *California Fed. Bank v. United States*, 39 Fed. Cl. 753, 754, 767 (1997).

NDIA's members are not "insane," and, absent this Court's review, they will be forced to place significant weight on the ruling below when deciding whether to enter into new contracts and on what terms.

2. Nor should there be any doubt as to the significance of the ruling on government operations. As staggering as the multi-billion dollar forfeiture is here, it represents only a small fraction of the

Department of Defense's overall annual investment in government contracts. In 2008, the Department of Defense dedicated more than $200 billion in *services* contracts alone. *See* GAO, Report No. 10-39, *Defense Acquisitions: Further Actions Needed to Address Weaknesses in DOD's Management of Professional and Management Support Contracts*, at "Highlights" (Nov. 2009). And for defense weapon programs, like those at issue in this case, the Department of Defense has planned to invest nearly $900 billion over the next 5 years the highest level in two decades. *See* GAO, Report No. 08-467SP, *Defense Acquisitions: Assessment of Selected Weapons Programs* 1 (Mar. 2008). These staggering investments by the government undermine any argument that the ruling below can be limited to the facts of this particular case. The hundreds of billions of dollars invested in numerous contracts many of which involve significant research and development like the contract at issue here virtually guarantees that these issues will arise again with frequency.

Indeed, the ruling below will discourage contractors from entering new contracts, which will ultimately harm the government, as it will be unable "to obtain needed goods and services" that contractors provide. *United States v. Winstar Corp.*, 518 U.S. 839, 913 (1996) (Breyer, J., concurring). This will occur at a time when the government can ill afford any such reduction, as contracted services extend far beyond weapons defense programs. Contractors are increasingly relied on "to perform core agency

missions." GAO, Report No. 08-572T, *Defense Management: DOD Needs to Reexamine Its Extensive Reliance on Contractors and Continue to Improve Management and Oversight*, at "Highlights" (Mar. 2008). Contractors are used in various roles for a number of operations, such as those in Iraq and Afghanistan. *See* GAO, Report No. 10-492, *Warfighter Support: DOD Needs to Improve Its Planning for Using Contractors to Support Future Military Operations*, at "Highlights" (Mar. 2010). As of November 2009, there were about 218,000 contractor employees operating in Iraq and Afghanistan a number that "at times exceed[ed] the number of military personnel in each country." *Ibid.* And the Department of Defense expects to continue this heavy reliance on contractors in the future. *Ibid.*

3. Perhaps even more significant is the *type* of contract the Federal Circuit's decision discourages. The ruling significantly undermines the flexibility in contracts needed for major research and development projects, which often have formed the backbone of the Nation's cutting-edge innovation, and which often are entered to counter a military threat.

When the goal is an uncharted innovation, it is difficult to establish a clear timeline for progress or completion. It is commonplace for government contracts to take longer than originally planned and to require more funding than originally expected. *See, e.g.*, GAO Report No. 09-326SP, *Defense Acquisitions*, *supra*, at 10-11 ("Only 28 percent of DoD's major defense acquisition programs currently estimate that

they will deliver on time or ahead of schedule, while just under one-half report they will have a delay of 1 year or more in delivery of an initial operational capability"); *id.* at 6 ("For DoD's 2008 programs, * * * the average delay in delivering initial capabilities is now 22 months"); GAO, Report No. 09-648T, *Space Acquisitions: Government and Industry Partners Face Substantial Challenges in Developing New DOD Space Systems*, at "Highlights" (Apr 2009) (noting problems that "had driven up costs and schedules"); GAO Report No. 08-467SP, *Defense Acquisitions, supra,* at 8 ("DOD has already missed fielding dates for many programs and many others are behind schedule."). Thus, the government frequently waives or excuses deadlines or requirements when the contract goal is more difficult to attain than initially contemplated, because the contract set "optimistic requirements for weapon programs that require new and unproven technologies." GAO Report No. 08-467SP, *Defense Acquisitions*, *supra*, at 24. But this government accommodation based on the government's own recognition that the contract goal (or, often, any research and development contract goal) cannot be completed in the time or under the specifications originally contemplated—should not provide the government with a justification to terminate the contract for default when it has waived or excused the very requirements that the contractor has not met. Indeed, the Federal Acquisition Regulation itself recognizes that "the work or methods" for "most R&D contracts * * * cannot be precisely described in advance." 48 C.F.R. § 35.002.

Notwithstanding this acknowledgement by the government, the government frequently cancels contracts because it has reallocated funding or other priorities. GAO Report No. 09-648T, *Space Acquisitions*, *supra*, at 1 (noting that DOD has canceled programs "that were expected to require investments of tens of billions of dollars"). Contractors understand such terminations for convenience are a matter of government prerogative, but before the ruling below they did not view such shifting priorities as a potential basis for a default termination. Without review by this Court, NDIA's members can ill afford to make that assumption, and undertaking future fixed-price development contracts may be "too great a risk" in most circumstances. Ralph C. Nash, *Fixed-Price Research & Development Contracts: A Risk Too High*, 23 Nash & Cibinic Rep. ¶ 39 (Aug. 2009).

CONCLUSION

For the foregoing reasons and in the petitions for a writ of certiorari, the petitions should be granted.

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JOINT APPENDIX

Nos. 09-1298 & 09-1302

IN THE

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preme Court, U.S.
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GENERAL DYNAMICS CORPORATION,
Petitioner,
v.
UNITED STATES OF AMERICA,
Respondent.

THE BOEING COMPANY,
Petitioner,
v.
UNITED STATES OF AMERICA,
Respondent.

On Writ Of Certiorari To The
United States Court Of Appeals
For The Federal Circuit

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Judgment (Fed. Cl. Aug. 31, 2001) 1262

Order (Fed. Cl. Oct. 4, 2001) 1263

Brief For Defendant-Appellee-Cross-Appellant, excerpt pages i-iii, 16-21, 52-70 (Fed. Cir. May 24, 2002) 1265

Judgment (Fed. Cl. May 3, 2007) 1293

NOTICE

The following documents have been omitted in the printing of this Appendix. They may be found in the No. 09-1298 Petitioner's Appendix at the following pages:

Appendix A
McDonnell Douglas Corp. v. United States, 567 F.3d 1340 (Fed. Cir. 2009) 1a

Appendix B
McDonnell Douglas Corp. v. United States, 76 Fed. Cl. 385 (2007) 35a

Appendix C
McDonnell Douglas Corp. v. United States, 323 F.3d 1006 (Fed. Cir. 2003) 178a

Appendix D
McDonnell Douglas Corp. v. United States, 50 Fed. Cl. 311 (2001) 212a

Appendix E
McDonnell Douglas Corp. v. United States, 182 F.3d 1319 (Fed. Cir. 1999) 250a

Appendix F
McDonnell Douglas Corp. v. United States, 40 Fed. Cl. 529 (1998) 280a

Appendix G
McDonnell Douglas Corp. v. United States, 37 Fed. Cl. 270 (1996) 343a

Appendix H
McDonnell Douglas Corp. v. United States, 35 Fed. Cl. 358 (1996) 382a

Appendix I

McDonnell Douglas Corp. v. United States, 29 Fed. Cl. 791 (1993) 430a

Appendix J

Order denying rehearing, *McDonnell Douglas Corp. v. United States*, No. 2007-5111 (Fed. Cir. Nov. 24, 2009) 444a

Appendix K

Statutory and Regulatory Provisions Involved 446a

Relevant Docket Entries

United States Court of Federal Claims
MCDONNELL DOUGLAS, et al v. USA
CIVIL DOCKET FOR CASE #: 1:91-cv-01204-RHH

DATE	#	DOCUMENT
06/07/1991	1	Complaint.
08/07/1991		Defendant's Motion to Dismiss.
08/14/1991		Defendant's Motion for the Designation of a Court Security Officer and Alternate Court Security Officers.
08/15/1991		Order.
08/22/1991		Notice of Filing of Classified Supplement to Complaint.
09/06/1991		Hearing Transcript.
09/12/1991		Plaintiffs' Motion for Leave to Amend Complaint and Amended Complaint.
09/13/1991		Hearing Transcript.
09/16/1991		Plaintiffs' Opposition to Defendant's Motion to Dismiss.
09/16/1991		Defendant's Response to Plaintiff's Motion for Leave to Amend Complaint.
09/16/1991		Order.

DATE	#	DOCUMENT
10/07/1991		Defendant's Reply to Plaintiffs' Opposition to Motion to Dismiss and Appendix.
11/22/1991		Defendant's Motion for Leave to File a Supplemental Brief in Support of Its Motion to Dismiss (Brief Attached).
12/04/1991		Plaintiffs' Motion for a Protective Order Regarding Classified Information and Memorandum in Support of Plaintiffs' Motion for a Protective Order Regarding Classified Information.
12/18/1991		Hearing Transcript.
12/18/1991		Order.
12/19/1991		Defendants' Motion for Leave to File Declaration of Peter Eames.
12/20/1991		Defendant's Cross-Motion for a Protective Order Regarding Classified Information.
01/09/1992		Plaintiffs' Opposition to Defendant's Cross-Motion and Reply to Defendant's Opposition to Plaintiffs' Motion for a Protective Order Regarding Classified Information.
01/10/1992		Plaintiffs' Response to Court's Draft of Joint Protective Order Governing Classified Information.

DATE	#	DOCUMENT
01/10/1992		Defendant's Response to Court's Draft of Joint Protective Order Governing Classified Information.
02/20/1992		Opinion and Order Denying Defendant's Motion to Dismiss.
03/20/1992		Defendant's Answer and Affirmative Defenses.
04/01/1992		Defendant's Motion to Dismiss Plaintiffs' Claims Related to "Superior Knowledge" in Alleged Other Low Observable Weapons Programs and Notice of Classified Filing in Support Thereof.
04/09/1992		Plaintiffs' Motion to Strike Affirmative Defenses or for a More Definite Statement of the Affirmative Defense of Setoff.
04/22/1992		Defendant's Response to Plaintiffs' Motion to Strike Affirmative Defenses or for a More Definite Statement of the Affirmative Defense of Setoff.

DATE	#	DOCUMENT
05/01/1992		Plaintiff's Brief in Response to Defendant's Motion to Dismiss Plaintiffs' Claims Related to "Superior Knowledge" in Alleged Other Low Observable Weapons Programs and Notice of Filing of Classified Appendix in Support Thereof.
05/01/1992		Plaintiff's Motion for Leave to Commence Discovery on Superior Knowledge Counts.
05/04/1992		Hearing Transcript.
05/08/1992		Notice of Filing of Classified Brief.
05/22/1992		Defendant's Reply to Plaintiff's Opposition to Defendant's Motion to Dismiss Plaintiffs' Claims Related to "Superior Knowledge" in Alleged Other Low Observable Weapons Programs.
05/22/1992		Defendant's Opposition to Plaintiff's Motion for Leave to Commence Discovery on Superior Knowledge Counts.
06/02/1992		Plaintiffs' Reply to Defendant's Opposition to Plaintiff's Motion for Leave to Commence Discovery on Superior Knowledge Counts.
06/03/1992		Notice of Classified Filing.

DATE	#	DOCUMENT
06/08/1992		Hearing Transcript.
06/15/1992		Hearing Transcript.
06/16/1992		Order.
07/16/1992		Order.
07/24/1992		Defendant's Motion for a Protective Order Regarding Discovery on "Superior Knowledge."
07/28/1992		Plaintiffs' Motion for Entry of an Order Governing Superior Knowledge Discovery and Brief in Opposition to Defendant's Motion for a Protective Order Regarding Discovery on "Superior Knowledge."
08/06/1992		Defendant's Reply to Plaintiffs' Opposition to Defendant's Motion for a Protective Order Regarding Discovery on "Superior Knowledge."
08/07/1992		Letter Regarding Count IX Hearing.
08/10/1992		Hearing Transcript.
08/12/1992		Plaintiffs' Motion for Leave to File Hearing Exhibits and Hearing Exhibits.
09/08/1992		Defendant's First Amended Answer and Affirmative Defenses.

DATE	#	DOCUMENT
09/09/1992		Defendant's Motion for a Stay of Discovery Regarding Superior Knowledge.
09/09/1992		Defendant's Motion for Leave to File and Defendant's Supplemental Brief Regarding Defendant's Motion for a Protective Order.
09/14/1992		Order.
09/16/1992		Plaintiff's Opposition to Defendant's Motion for Leave to File and Defendant's Supplemental Brief Regarding Defendant's Motion for a Protective Order.
09/17/1992		Defendant's Motion to Certify Order for Interlocutory Appeal.
09/17/1992		Defendant's Motion for Leave to File and Defendant's Supplement to Defendant's Supplemental Brief Regarding Defendant's Motion for a Protective Order.
09/18/1992		Hearing Transcript.
09/29/1992		Plaintiff's Motion to Compel Discovery.
10/05/1992		Plaintiffs' Brief in Opposition to Government's Motion to Certify Order for Interlocutory Appeal.
10/08/1992		Hearing Transcript.

DATE	#	DOCUMENT
10/13/1992		Plaintiffs' Supplemental Brief in Support of Motion to Compel Discovery.
10/14/1992		Hearing Transcript (In Camera).
10/15/1992		Defendant's Reply to Plaintiffs' Opposition to Defendant's Motion to Certify Order for Interlocutory Appeal.
10/29/1992		Defendant's Response to Plaintiffs' Supplemental Brief in Support of Motion to Compel Discovery.
10/30/1992		Order.
11/05/1992		Hearing Transcript.
11/12/1992		Defendant's Response to the Court's Order of October 30, 1992.
11/13/1992		Plaintiffs' Motion to Compel Discovery.
11/17/1992		Notice of Filing of Classified Appendix.
11/20/1992		Plaintiffs' Supplemental Brief Regarding Plaintiffs' Motion to Compel Discovery.
11/22/1992		Defendant's Response to Plaintiff's Motion to Compel of November 13, 1992.
11/23/1992		Hearing Transcript.

DATE	#	DOCUMENT
11/23/1992		Order and Opinion Denying Request to Certify for Interlocutory Appeal.
11/23/1992		Protective Order.
11/23/1992		Order.
12/02/1992		Order.
01/23/1993		Hearing Transcript and Order that Hearing Transcript Shall Not Be Duplicated Except By Order of the Court.
02/05/1993		Stipulation and Protective Order.
02/08/1993		Defendant's Motion for a Protective Order.
02/09/1993		Plaintiffs' Motion for Leave to File Second Amended Unclassified Complaint.
02/09/1993		Defendant's Motion for a Protective Order and Response to Plaintiffs' Motion to Compel Responses to Discovery Requests Withheld Under Claim of Discovery Stay.
02/12/1993		Plaintiffs' Motion for an Order Governing B-2 and F-117a Discovery.

DATE	#	DOCUMENT
02/17/1993		Plaintiffs' Response to Defendant's Motion for a Protective Order and Reply to Defendant's Response to Plaintiffs' Motion to Compel Responses Withheld Under a Claim of Discovery Stay.
02/18/1993		Opinion and Order Denying Motion to Dismiss and Vacating All Stays of Discovery.
02/25/1993		Defendant's Response to Plaintiffs' Motion for an Order Governing B-2 and F-117a Discovery.
02/26/1993		Hearing Transcript.
03/01/1993		Order.
03/03/1993		Order.
03/03/1993		Defendant's Motion for Partial Reconsideration of the Court's Order Dated March 1, 1993.
03/05/1993		Order.
03/05/1993		Plaintiffs' Supplemental Memorandum in Support of their Motion to Compel Production.
03/08/1993		Defendant's Motion for a Stay of Court's March 5, 1993 Order.
03/09/1993		Order Denying Motion for a Stay.

DATE	#	DOCUMENT
03/09/1993		Petition for Writ of Mandamus and Motion for a Stay Pending Resolution of Petition for Writ of Mandamus.
03/09/1993		Order of Court of Appeals for the Federal Circuit.
03/10/1993		Defendant's Second Amended Unclassified Answer and Affirmative Defenses.
03/10/1993		Plaintiffs'-Respondents' Opposition to the Government's Motion for a Stay Pending Resolution of the Government's Petition for a Writ of Mandamus.
03/11/1993		Defendant-Petitioner's Reply to Plaintiffs'-Respondents' Opposition to the Government's Motion to Stay.
03/12/1993		Order of Court of Appeals for the Federal Circuit.
03/16/1993		Plaintiffs'-Respondents' Opposition to Petition for Writ of Mandamus and Appendix in Support Thereof [Misc. No. 370].
03/17/1993		Defendant-Petitioner's Reply to Plaintiffs'-Respondents' Opposition to Petition for Writ of Mandamus [Misc. No. 370].

DATE	#	DOCUMENT
03/18/1993		Plaintiffs'-Respondents' Sur-Reply to Defendant-Petitioner's Reply to Petition for Writ of Mandamus [Misc. No. 370].
03/18/1993		Order.
03/23/1993		Hearing Transcript.
03/23/1993		Order.
03/30/1993		Notice of Filing of Classified Ex Parte In Camera Declaration.
03/30/1993		Defendant's Motion for a Protective Order.
03/31/1993		Order.
04/01/1993		Defendant's Supplemental Brief in Support of Motion for Protective Order.
04/02/1993		Hearing Transcript.
04/03/1993		Defendant's Second Supplemental Brief in Support of Motion for Protective Order.
04/06/1993		Defendant's Second Supplemental Brief in Support of Motion for a Protective Order.
04/06/1993		Defendant's Notice of Filing of Classified In Camera Ex Parte Declaration and Materials.
04/07/1993		Order.

DATE	#	DOCUMENT
04/08/1993		Order.
04/09/1993		Plaintiff's Opposition to Defendant's Motion for a Protective Order Barring Access to Unnamed Classified Programs and Notice of Filing of Classified Appendix in Support Thereof.
04/09/1993		Plaintiff's Notice of Filing of Classified Deposition Transcript.
04/09/1993		Plaintiffs' Motion for Leave to File an In Camera Classified Declaration.
04/12/1993		Order.
04/13/1993		Defendant's Reply to Plaintiff's Opposition to Defendant's Motion for a Protective Order.
04/13/1993		Defendant's Motion for Stay of Order Pending Interlocutory Appeal and Motion to Certify Order for Interlocutory Appeal.
04/14/1993		Order Denying Motion to Stay.
04/14/1993		Order Denying Motion to Certify for Interlocutory Appeal.
04/15/1993		Government's Petition for Mandamus and Request for Stay to the Court of Appeals for the Federal Circuit.
04/16/1993		Order.

DATE	#	DOCUMENT
04/16/1993		Plaintiffs' Motion Requesting Record of In Camera Proceedings.
04/16/1993		Court of Appeals for the Federal Circuit Order.
04/20/1993		Court of Appeals for the Federal Circuit Order.
04/20/1993		Order.
04/21/1993		Defendant's Response to the Court's Order Dated April 16, 1993 [Misc. No. 370].
04/21/1993		Plaintiffs'-Respondents' Opposition to Petition for Writ of Mandamus and Opposition to a Stay Pending Resolution of Petition and Motion for Leave to File Documents In Camera [Misc. No. 370].
04/22/1993		Defendant-Petitioner's Reply to Plaintiffs'-Respondents' Opposition to Petition for Writ of Mandamus and Opposition to a Stay [Misc. No. 370].
04/27/1993		Order.
04/30/1993		Order.
04/30/1993		Court of Appeals for the Federal Circuit Order.
05/05/1993		Order.

DATE	#	DOCUMENT
05/07/1993		Order Staying All Discovery on Air Force Programs.
05/20/1993		Order.
05/26/1993		Plaintiffs' Memorandum Concerning Continuation of Discovery on Count IX and Notice of Filing of Classified Appendix in Support Thereof.
05/27/1993		Defendant's Motion to Dismiss Plaintiff's Superior Knowledge Claims, Or In the Alternative for Partial Summary Judgment, and Motion for a Protective Order and Notice of Filing of Classified Appendix in Support Thereof.
05/27/1993		Defendant's Memorandum Regarding "Superior Knowledge" Hearing on May 28.
06/08/1993		Plaintiff's Motion for Continuance of Defendant's Motion for Partial Summary Judgment.
06/10/1993		Hearing Transcript.
06/11/1993		Defendant's Response to Plaintiff's Motion for a Continuance.
06/11/1993		Defendant's Notice of Filing of Classified, In Camera, Ex Parte Appendix to Motion to Dismiss Plaintiffs' Superior Knowledge Claims.

DATE	#	DOCUMENT
06/15/1993		Notice of Filing of Classified Appendix.
06/21/1993		Order.
06/21/1993		Opinion and Order.
06/23/2003		Defendant's Status Report Concerning Count IX.
06/25/1993		Plaintiff's Response to Status Report re Count IX.
07/08/1993		Order.
07/15/1993		Defendant's Status Report Concerning Count IX.
07/19/1993		Order Vacating Stay of Discovery on Superior Knowledge Claims.
07/23/1993		Defendant's Supplement to Motion to Dismiss Plaintiff's Superior Knowledge Claims.
07/26/1993		Opinion and Order.
08/11/1993		Order.
10/22/1993	3	TRANSCRIPT of proceedings re: 28 volumes, taken at Washington, D.C., for dates of September 20-30, 1993, and October 1, October 4, October 5, and October 7, 1993.

DATE	#	DOCUMENT
11/01/1993	5	PUBLISHED DECISION addressing state secrets doctrine and discovery issues, and setting concurrent Brief deadline to November 19, 1993.
11/19/1993	13	NOTICE of filing of classified, EX PARTE materials by USA.
11/19/1993	14	MEMORANDUM by USA re: motion to dismiss "Superior Knowledge" Claims, and response to 11/1/93 order.
11/22/1993	16	MEMORANDUM by MCDONNELL DOUGLAS, GENERAL DYNAMICS re: superior knowledge order by leave of the Judge.
11/29/1993	21	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS for Summary Judgment on Count IX.
11/29/1993	22	PROPOSED FINDINGS of Uncontroverted Fact by MCDONNELL DOUGLAS, GENERAL DYNAMICS.
11/29/1993	23	Notice of filing a classified appendix by MCDONNELL DOUGLAS, GENERAL DYNAMICS.
12/17/1993	54	RESPONSE by MCDONNELL DOUGLAS, GENERAL DYNAMICS to response by USA.

DATE	#	DOCUMENT
12/20/1993	58	RESPONSE by MCDONNELL DOUGLAS, GENERAL DYNAMICS to USA's memorandum [i.e. motion to dismiss "Superior Knowledge" claims] by leave of the Judge.
12/23/1993	64	ORDER entered directing the Clerk to refuse to accept for filing any pleadings signed by or for the current attorney of record for the USA or the Director of Commercial Litigation until further direction from the court.
12/29/1993		Attorney for defendant, Mary Sue Mitchellson, terminated this date.
01/03/1994	68	MOTION by USA For reconsideration of order under Rule 83.2 , to Vacate order, and for Expedited Consideration.
01/03/1994	73	Notice of filing classified materials by USA.
01/03/1994	74	CROSS MOTION to Dismiss by USA and RESPONSE to motion for Summary Judgment by GENERAL DYNAMICS, MCDONNELL DOUGLAS.
01/03/1994	75	STATEMENT OF GENUINE ISSUES by USA.

DATE	#	DOCUMENT
01/10/1994	78	REPLY by USA to plaintiffs' 12/17/93 brief in response to USA'S motion to dismiss plaintiffs' Superior Knowledge Claims.
01/10/1994	79	ORDER granting motion to Extend Time to respond to motion for summary judgment.
01/31/1994	87	Notice of filing classified appendix by MCDONNELL DOUGLAS, GENERAL DYNAMICS.
02/01/1994	89	REPLY by MCDONNELL DOUGLAS, GENERAL DYNAMICS to response to cross motion.
02/01/1994	90	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS for Leave to File a supplemental superior knowledge memorandum regarding Northrop ATA proposal documents.
02/02/1994	94	ORDER granting [90-1] motion for Leave to File a supplemental superior knowledge memorandum.
02/02/1994	95	SUPPLEMENTAL MEMORANDUM by MCDONNELL DOUGLAS, GENERAL DYNAMICS re: Northrop ATA Proposal Documents PLACED IN CAMERA.

DATE	#	DOCUMENT
02/04/1994	118	TRANSCRIPT of proceedings re: 1 volume, at Washington, D.C., for date of February 3, 1994. Notice to parties.
02/04/1994	97	ORDER entered that there is no basis for finding that the Air Force acted to help or hinder development of the merits of this case, with the Clerk directed to accept any pleadings complying with the Rules from the USA.
02/10/1994	102	STATUS REPORT by USA.
02/14/1994	109	REPLY by USA to response to cross-motion.
02/16/1994	113	ORDER scheduling Show Cause Hearing for 10:00 a.m. on 3/7/94 for USA to Show Cause why the Court should not deem admitted plaintiffs' superior knowledge claims, etc.
02/18/1994	122	ORDER denying motion For reconsideration of order under Rule 83.2. Order also states that the December 23, 1993 order is now MOOT.
03/07/1994		Show Cause Hearing held.
03/07/1994	141	MOTION by USA for Leave to File response to order to show cause, and response to order to show cause.

DATE	#	DOCUMENT
03/09/1994	143	ORDER re: defendant's response to order to show cause.
03/23/1994	155	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS for Leave to File reply, and reply to defendant's response to Show Cause Order on Superior Knowledge.
03/24/1994	159	ORDER entered directing plaintiffs to designate representatives to explore feasibility of proposal to litigate portion of superior knowledge case, etc.
03/28/1994	163	MOTION by USA for Reconsideration of order.
03/31/1994	167	ORDER adding matters to agenda for a show cause hearing.
04/04/1994	172	STATUS REPORT re: assertion of privileges by USA
04/05/1994	173	RESPONSE by MCDONNELL DOUGLAS, GENERAL DYNAMICS to report by USA.
04/14/1994	189	ORDER entered re further procedures.
04/18/1994	195	STATUS REPORT regarding Count IX by USA.
04/20/1994	201	ORDER entered re: security issues related to Count 9.

DATE	#	DOCUMENT
04/28/1994	219	ORDER entered re discovery, etc.
07/22/1994	312	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS for Leave to File to permit disclosure of nonparty B-2 and F-117A information to plaintiffs' engineers cleared into those programs.
07/28/1994	317	ORDER entered granting motion for Leave to File to permit disclosure of non-party B-2 and F-117A information to plaintiffs' engineers cleared into those programs.
09/14/1994	341	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS to Compel discovery of documents from the B-2 and F- 117A programs.
09/23/1994	347	RESPONSE by USA to motion to Compel.
09/27/1994	345	TRANSCRIPT of proceedings re: 1 volume, at Washington, D.C., for date of September 26, 1994.
09/26/1994	354	ORDER entered that plaintiff's motion to compel discovery is suspended pending a review by government counsel of the Air Force response to plaintiff's interrogatories and request for production.

DATE	#	DOCUMENT
10/04/1994	361	STATUS REPORT by USA re: production of documents from the B-2 and F-117A programs.
10/04/1994	360	MOTION by MCDONNELL DOUGLAS for entry of B-2 and F-117A discovery order.
10/04/1994	361	STATUS REPORT by USA re: production of documents from the B-2 and F-117A programs.
10/14/1994	364	ORDER set Evidentiary Hearing to discuss B-2 and F-117A discovery: 10:00 a.m. on 10/17/94.
10/17/1994	365	TRANSCRIPT of proceedings re: 1 volume, at Washington, D.C. for date of October 17, 1994.
11/01/1994	377	(Preliminary) STATUS REPORT by USA re: production of documents from the B-2 program.
11/02/1994	380	ORDER entered re apparent destruction of documents etc. (signed by Judge Robert H. Hodges).
11/03/1994	378	ORDER granting motion for Leave to File revised preliminary status report regarding production of B-2 documents.

DATE	#	DOCUMENT
11/03/1994	402	REVISED PRELIMINARY STATUS REPORT regarding production of documents from the B-2 program by USA.
11/16/1994	384	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS for Leave to File response to defendant's status report re: the production of B-2 documents.
11/16/1994	385	STATUS REPORT by USA.
11/18/1994	403	RESPONSE by MCDONNELL DOUGLAS, GENERAL DYNAMICS to report by USA.
12/01/1994	391	ORDER granting motion for leave re: production of B-2 documents, etc.
12/09/1994	393	ORDER directing parties of Judge's decision of agreement with Plaintiff re: improper termination of A-12 contract for default in Count XVII.
12/16/1994	400	ORDER granting motion for entry of B-2 and F-117A discovery order.
01/31/1995	424	ORDER entered that defendant will have the opportunity at trial to present evidence that contractor performance was so deficient at the time of termination.

DATE	#	DOCUMENT
02/07/1995	435	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS to Compel production of documents related to classified supporting data file UNDER SEAL IN CAMERA.
02/22/1995	449	RESPONSE by USA to motion to Compel production of documents related to classified supporting data. FILED UNDER SEAL.
03/07/1995	453	REPLY by MCDONNELL DOUGLAS, GENERAL DYNAMICS to response to motion to Compel production of documents related to classified supporting data. FILED UNDER SEAL.
03/09/1995	459	ORDER directing parties of further procedures to take if discovery cannot be resolved.
03/23/1995	481	ORDER Staying briefing schedule for Plaintiff's summary judgment motion and addressing other case proceedings.
04/07/1995	488	ORDER entered re further proceedings.
12/19/1995	793	ORDER set Brief [parties' proposed schedule for addressing damages] deadline to 1/5/96.

DATE	#	DOCUMENT
01/05/1996	794	MOTION by USA for entry of case management order to address damages aspects of this case.
01/05/1996	795	MOTION by USA to Dismiss Damages Allegations and for Entry of a Partial Final Judgment or, in the Alternative, for Certification for Interlocutory Appeal.
01/05/1996	796	STATUS REPORT (Proposed Schedule for Addressing Damages) by MCDONNELL DOUGLAS, GENERAL DYNAMICS.
01/23/1996	800	ORDER Response to motion to Dismiss Damages Allegations and for Entry of a Partial Final Judgment or, in the Alternative, for Certification for Interlocutory Appeal reset to 1/26/96 and Reply to Response to Motion reset to 2/2/96 for motion to Dismiss Damages Allegations and for Entry of a Partial Final Judgment or, in the Alternative, for Certification for Interlocutory Appeal.
01/25/1996	801	RESPONSE by USA to motion for entry of case management order to address damages aspects of this case.

DATE	#	DOCUMENT
01/26/1996	803	RESPONSE by MCDONNELL DOUGLAS, GENERAL DYNAMICS to motion to Dismiss Damages Allegations and for Entry of a Partial Final Judgment or, in the Alternative, for Certification for Interlocutory Appeal.
02/07/1996	808	REPLY by USA to response to motion to Dismiss Damages Allegations and for Entry of a Partial Final Judgment or, in the Alternative, for Certification for Interlocutory Appeal.
02/07/1996	809	REPLY TO RESPONSE by MCDONNELL DOUGLAS and GENERAL DYNAMICS to response by USA.
02/07/1996	811	ORDER re: further procedures.
02/29/1996	827	MOTION by MCDONNELL DOUGLAS for Leave to File under seal its memorandum on superior knowledge discovery in response to the court's 2/7/96 Order.
02/29/1996	828	STATUS REPORT (Regarding Superior Knowledge Discovery and the Order of Proof at Trial), by GENERAL DYNAMICS.

DATE	#	DOCUMENT
02/29/1996	829	ORDER granting motion for Leave to File under seal its memorandum on superior knowledge discovery in response to the court's 2/7/96 Order.
03/01/1996	831	MEMORANDUM by MCDONNELL DOUGLAS re: superior knowledge discovery per order with one volume appendix filed by leave of the Judge AND PLACED IN CAMERA.
03/18/1996	837	ORDER set Evidentiary Hearing for discovery in the B-2 program: 10:00 a.m. on 3/22/96.
03/20/1996	839	RESPONSE by USA to report by GENERAL DYNAMICS by leave of the Judge.
03/22/1996	841	ORDER set Additional Documents issues of burden of proof and sequence of procedures, etc. [brief] due: 4/1/96 for USA, 4/8/96 [response to brief] for GENERAL DYNAMICS and MCDONNELL DOUGLAS.
03/25/1996	842	TRANSCRIPT of proceedings re: 1 volume, at Washington, D.C., for date of March 22, 1996.
04/02/1996	845	RESPONSE (filed as defendant's supplemental brief concerning the burden of proof, the order for presentation of evidence at trial, and pretrial schedule) by USA to order.

DATE	#	DOCUMENT
04/08/1996		Petition for a Writ of Mandamus.
04/08/1996	851	PUBLISHED DECISION.
04/09/1996	852	RESPONSE by MCDONNELL DOUGLAS, GENERAL DYNAMICS to response by USA.
04/19/1996	859	Additional Documentation [supplement to memorandum in response to the order dated April 3, 1996] by USA and placed in camera.
04/19/1996	860	MEMORANDUM by USA re: order.
04/19/1996	861	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS for a pretrial determination that no loss adjustment can apply, etc.
04/19/1996	862	Additional Documentation [supplemental appendix to plaintiffs' motion for a pretrial, etc.] by MCDONNELL DOUGLAS and GENERAL DYNAMICS and placed in camera.
05/02/1996		Answer to Petition for Writ of Mandamus.
05/06/1991	871	TRANSCRIPT of proceedings re: pre-trial conference, 1 volume, at Washington, D.C., for date of May 3, 1996.

DATE	#	DOCUMENT
05/13/1996	875	ORDER directing counsel to meet no later than May 24, 1996 to perform tasks as outlined in said order and directing counsel to notify court of the results of said meeting as soon as possible.
05/16/1996	878	ORDER Clarifying case status and court's position.
05/17/1996	879	ORDER addressing case proceedings and upcoming trial and hearing.
05/24/1996	889	RESPONSE by USA to motion for a pretrial determination that no loss adjustment can apply, etc.
05/31/1996		Court of Appeals for the Federal Circuit Order Denying Petition for Mandamus.
06/05/1996		Oral Argument re: motion for a pretrial determination that no loss adjustment can apply, etc. by GENERAL DYNAMICS, MCDONNELL DOUGLAS.
06/05/1996	894	TRANSCRIPT of proceedings re: 1 volume, at Washington, D.C., for date of June 5, 1996 exhibits:

DATE	#	DOCUMENT
06/12/1996	897	ORDER directing parties the only issue for determination of damages is incurred costs, closing discovery that is not related to incurred costs and directing parties all other discovery deadlines remain in effect unless they are changed by agreement of counsel or order of court and set Trial or hearing for 9/16/96.
06/13/1996	902	TRANSCRIPT of proceedings re: 1 volume, at Washington, D.C., for date of June 12, 1996.
09/25/1996	999	MOTION by MCDONNELL DOUGLAS for Leave to File UNDER SEAL its proposed findings of fact and conclusions of law supporting non-imposition of a lost ratio.
10/09/1996	1003	ORDER granting motion for Leave to File UNDER SEAL its proposed findings of fact and conclusions of law supporting non-imposition of a loss ratio.
10/09/1996	1006	RESPONSE by USA to Motion for Leave to File UNDER SEAL its proposed findings of fact and conclusions of law supporting non-imposition of a lost ratio.
10/22/1996	1012	RESPONSE by GENERAL DYNAMICS to order.

DATE	#	DOCUMENT
11/26/1996	1019	MOTION by GENERAL DYNAMICS regarding preservation of record for appeal.
12/09/1996	1022	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS for a determination of the balance due plaintiffs from the government.
12/13/1996	1026	PUBLISHED DECISION.
01/22/1997	1041	PUBLISHED DECISION granting in part, denying in part motion to Dismiss Damages Allegations and for Entry of a Partial Final Judgment or, in the Alternative, for Certification for Interlocutory Appeal.
02/05/1997	1044	PUBLISHED DECISION denying motion for Summary Judgment.
07/23/1997	1095	TRANSCRIPT of proceedings re: 25 volumes, taken at Washington, DC, for date of June 17 through July 14, 1997, together with cumulative index.
08/14/1997	1098	Post-trial (memorandum of contentions of fact and law) by USA.
08/14/1997	1099	FINDINGS OF FACT AND CONCLUSIONS OF LAW by MCDONNELL DOUGLAS, GENERAL DYNAMICS.
02/20/1998	1128	PUBLISHED DECISION.

DATE	#	DOCUMENT
03/30/1998	1147	PUBLISHED DECISION vacating the published Opinion and Order, vacating the judgment, and directing Clerk to enter judgment accordingly.
03/31/1998	1148	JUDGMENT entered pursuant to Rule 58 awarding plaintiffs the sum of $1,200,132,820.00, plus statutory interest from June 26, 1991, until paid. No costs.
04/02/1998	1150	NOTICE OF APPEAL by USA.
05/29/1998	1154	NOTICE OF CROSS-APPEAL by GENERAL DYNAMICS.
05/29/1998	1155	NOTICE OF CROSS-APPEAL by MCDONNELL DOUGLAS.
6/27/2000		Status Conference held (no reporter requested).
7/18/2000	1159	NOTICE of Statement of Issues and Notice of Probable Testifying Experts for Trial by USA.
7/31/2000	1160	RESPONSE by MCDONNELL DOUGLAS and GENERAL DYNAMICS to notice by USA.
08/11/2000	1162	ORDER set hearing for 10:00 a.m., 9/6/00.

DATE	#	DOCUMENT
8/11/2000	1163	TRANSCRIPT of proceedings re: Status Conference, 1 volume, at Washington, D.C., for date of August 10, 2000.
9/29/2000	1169	TRANSCRIPT of proceedings re: Evidentiary Hearing, 1 volume, at Washington, D.C., for date of September 28, 2000.
11/07/2000	1177	ORDER set Status Conference for 10:00 a.m., 11/16/00.
12/15/2000	1182	STATUS REPORT by USA.
12/19/2000	1888	STATUS REPORT by MCDONNELL DOUGLAS and GENERAL DYNAMICS.
12/21/2000	1192	TRANSCRIPT of proceedings, 1 volume, at Washington, D.C., for date of December 19, 2000.
01/12/2001	1197	MOTION by USA to Compel disclosure of plaintiff's case and brief in support, (together with separate appendix).
01/31/2001	1207	RESPONSE by MCDONNELL DOUGLAS, GENERAL DYNAMICS to motion to Compel disclosure of plaintiff's case and brief in support, filed with a (1) one volume appendix.

DATE	#	DOCUMENT
02/07/2001	1210	NOTICE of an Ex Parte filing in connection with Plaintiff's 29th and 30th sets of discovery requests by USA.
02/09/2001	1213	REPLY by USA to response to motion to Extend Time within which respond to motion to compel disclosure of plaintiff's case.
02/12/2001	1212	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS to Extend Time to file briefs re: issues to be tried (pending determination of government's invocation of state secrets privilege) and for a status conference.
02/12/2001	1217	RESPONSE by USA to motion to Extend Time to file briefs re: issues to be tried.
02/12/2001	1218	Brief regarding issues to be addressed and the appropriate trial standards to be applied at the May 1, 2001, default trial filed by USA.
02/15/2001	1215	ORDER Status Conference for 10:00 a.m., 2/23/01.
02/21/2001	1219	TRANSCRIPT of proceedings 1 volume, at Washington, D.C., for date of February 20, 2001. Notice to parties.

DATE	#	DOCUMENT
03/01/2001	1229	UNPUBLISHED DECISION reaffirming the December 13, 1996 opinion and order; and concluding that defendant may not obtain a lost adjustment pursuant to FAR 49.203, and plaintiffs may not obtain profits pursuant to FAR 49.202.
03/07/2001	1236	STATEMENT OF ISSUES AND LEGAL STANDARDS FOR TRIAL by MCDONNELL DOUGLAS and GENERAL DYNAMICS
03/28/2001	1264	MOTION, together with four volumes of appendix, by USA For reconsideration of order under Rule 83.2 and brief regarding effect of state secrets.
03/30/2001	1269	TRANSCRIPT of proceedings re: Evidentiary Hearing, 1 volume, at Washington, D.C., for date of March 29, 2001. .
04/10/2001	1277	NOTICE of Supplemental Authority by USA.

DATE	#	DOCUMENT
4/27/2001	1284	ORDER denying motion For reconsideration of order under Rule 83.2. Trial of this case begins at 10:00 a.m. on May 7 and 9:00 a.m. thereafter until June 29. The court will not meet on May 28 or June 4-8. The time will be evenly divided between plaintiffs and defendant. Mr. Lewis is excluded as an expert witness. See Transcript of hearing on April 23, 2001. All other motions that were pending and not listed on the April 23 proposed agenda and status report are moot and thereafter denied.
04/30/2001	1285	TRANSCRIPT of proceedings re: Pre-Trial Conference, 1 volume (151 pages), at Washington, D.C., for date of April 23, 2001.
07/10/2001	1330	Post-trial brief filed by MCDONNELL DOUGLAS.
07/10/2001	1331	PROPOSED FINDINGS OF FACT filed by MCDONNELL DOUGLAS.
07/10/2001	1329	PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW filed BY GENERAL DYNAMICS.
07/11/2001	1333	Post-trial brief by USA.

DATE	#	DOCUMENT
08/31/2001	1346	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS to Stay this Court's Judgment in light of Defendant's recent collection report.
08/31/2001	1347	JUDGMENT entered, pursuant to Rule 58, that the complaint is dismissed and judgment is entered in favor of defendant. No costs.
09/17/2001	1351	MOTION by MCDONNELL DOUGLAS (Service by hand: 9/17/01) to Amend judgment order.
09/17/2001	1352	MOTION by GENERAL DYNAMICS to Alter Judgment, and to Amend to Court's findings.
10/04/2001	1353	ORDER denying motion to Alter Judgment, motion to Amend to Court's findings and motion to Amend judgment order.
11/16/2001	1356	MOTION by MCDONNELL DOUGLAS, GENERAL DYNAMICS to Stay Government's collection demand.
11/21/2001	1357	RESPONSE by USA to motion to Stay Government's collection demand.

DATE	#	DOCUMENT
11/26/2001	1358	ORDER re: Directing parties to agree on a date and time to address the Court's responsibilities in this matter concerning the money judgment, if the parties feel the Court has additional responsibilities.
11/30/2001	1359	NOTICE OF APPEAL by GENERAL DYNAMICS.
11/30/2001	1360	NOTICE OF APPEAL by MCDONNELL DOUGLAS
12/14/2001	1361	NOTICE OF CROSS-APPEAL by USA.
01/09/2004	1382	MOTION for Judgment Based Upon Additional Findings Mandated by the Court of Appeals and Memorandum in Support, Together with Separately Bound Supplemental Appendix (Volume I) by USA.
01/23/2004	1385	CROSS MOTION and OPPOSITION to Dft's Motion for Judgment on Partial Findings, Together with Separately Bound Appendix Volume by MCDONNELL DOUGLAS CORPORATION.

DATE	#	DOCUMENT
1/26/2004	1386	REPONSE to Motion for Judgment on Partial Findings and Motion for Judgment on Partial Findings by USA and CROSS MOTION for conversion of default termination to termination for convenience, together with 5 separate volumes of appendix, filed by GENERAL DYNAMICS CORPORATION.
03/12/2004	1393	OPPOSITION to Pltfs' CROSS MOTION for Judgment and Conversion of the Default Termination to Termination for Convenience and BRIEF IN REPLY to Pltfs' Responses to Dft's Motion for Judgment, Together with Four (4) Separately Bound Appendix Volumes, filed by USA.
04/16/2004	1397	REPLY to Response to Motion re CROSS MOTION to Motion for Judgment on Partial Findings filed by USA filed by MCDONNELL DOUGLAS CORPORATION.
4/16/2004	1398	Reply to Opposition to Motion for Conversion of Default Termination to Termination for Convenience, with a (1) one volume appendix in support.

DATE	#	DOCUMENT
7/15/2004	1408	SUPPLEMENTAL BRIEF and PROPOSED ADDITIONAL FINDINGS OF FACT by MCDONNELL DOUGLAS CORPORATION.
7/15/2004	1409	POINTS IN REBUTTAL to Pltfs' Oral Argument, filed by USA.
6/8/2006	1431	POST ARGUMENT BRIEF, filed by USA.
7/6/2006	1434	RESPONSE to MOTION to Amend Schedule re: Order on Motion for Extension of Time to File , filed by MCDONNELL DOUGLAS CORPORATION, GENERAL DYNAMICS CORPORATION.
7/21/2006	1438	MOTION for Leave to File Supplemental Brief in Reply To Plaintiffs' Response Brief, filed by USA.
5/3/2007	1440	PUBLISHED ORDER and OPINION granting 1382 Motion for Judgment on Partial Findings; denying 1385 Cross Motion; denying 1386 Cross Motion. The Clerk is directed to enter judgment.
05/03/2007	1441	JUDGMENT entered, pursuant to Rule 58, in favor of defendant. No costs.

Relevant Docket Entries

U.S. Court of Appeals for the Federal Circuit
MCDONNELL DOUGLAS CORP v. UNITED STATES
1998-5096

DATE	DOCUMENT
6/15/1998	Brief of Defendant-Appellant to the Federal Circuit.
8/3/1998	Brief of Plaintiffs-Cross Appellants' to the Federal Circuit.
9/28/1998	Reply and Cross-Appellee Brief of Defendant-Appellant to the Federal Circuit.
7/1/1999	Federal Circuit Opinion.

Relevant Docket Entries

U.S. Court of Appeals for the Federal Circuit
MCDONNELL DOUGLAS CORP v. UNITED STATES
2002-5034

DATE	DOCUMENT
3/6/2002	Brief for Plaintiff-Appellant General Dynamics the Federal Circuit.
3/6/2002	Brief for Plaintiff-Appellant McDonnell Douglas in the Federal Circuit.
5/24/2002	Brief for Defendant-Appellee-Cross-Appellant United States in the Federal Circuit.
7/31/2002	Reply/Cross-Appellee Brief for McDonnell Douglas in the Federal Circuit.
8/15/2002	Reply/Cross-Appellee Brief for General Dynamics in the Federal Circuit.
9/13/2002	Cross Reply Brief for Defendant-Appellee-Cross Appellant United States in the Federal Circuit.
3/17/2003	Federal Circuit Opinion.

Relevant Docket Entries

U.S. Court of Appeals for the Federal Circuit
MCDONNELL DOUGLAS CORP v. UNITED STATES
2007-5111

DATE	DOCUMENT
10/23/2007	Brief for Plaintiff-Appellant General Dynamics in the Federal Circuit.
10/23/2007	Brief for Plaintiff-Appellant McDonnell Douglas in the Federal Circuit.
02/19/2008	Brief for Defendant-Appellee United States in the Federal Circuit.
04/17/2008	Reply Brief for McDonnell Douglas in the Federal Circuit.
12/01/2009	Federal Circuit Opinion.

ASSISTANT SECRETARY OF DEFENSE
Washington, D.C. 20301-8000

5 Jan. 1988

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION

SUBJECT: ATA Risk Management

Subject 8118 of the FY88 DoD appropriations act requires that, before a fixed price type contract is used for development of a major system, the USD(A) make a written determination that risk has been reduced to enable realistic pricing and that the contract type permits an equitable and sensible allocation of program risk between the contracting parties.

I have had two hours to review the Navy ATA program which is employing a fixed price FSD contract and three years of not-to-exceed (NTE) prices for production. I, therefore, cannot give you a firm, well-reasoned recommendation regarding the two elements on which you must make your determination required by Section 8118 – that program risk has been reduced to the extent that realistic pricing can occur or whether program risk is equitably shared, but I can express some of my observations and reservations.

The Navy has selected a source and is very eager to sign a contract, hence their briefing may indicate that program risk is less than it actually is. The Navy does not consider technical risk to be high

with the exception of instability of the low observable design which has not been prototyped in a flying model. This will be the first carrier based low observable aircraft. First flight is scheduled for FY 90. The Navy plans to maximize use of existing avionics though the contractor will be required to design a new radar and conformal antennas and will have to modify F-404 engines. Software integration of the avionics will also be required. I cannot effectively evaluate the technical risk involved in these efforts in the short time available. The ceiling price of the FSD contract is $4.8B – the target cost is 20% below that at $4.0B with a 60%/40% share from target to ceiling making this a tightly priced FPI contract. The Navy appears to have adequately priced all known development costs and the in-house Government estimate is close to the proposed price. There is not an amount included for contingencies or for unforeseen technical problems that inevitably arise on major R&D programs. There is an economic adjustment clause to cover unusual inflation. The winning McDonnell/General Dynamics (GD) team's price was $800M lower than the Grumman/Northrop team's proposal. Northrop has had experience with low observables and McDonnell/GD have not so it could be the Northrop estimate was more realistic. McDonnell and GD are strongly interested in becoming involved in stealth technology so they might be prepared to accept some risks to do so.

The FSD contract includes 3 years of production NTE's amounting to $4.6B for 34 aircraft (6, 8 and 20). There is considerable risk in these NTE prices. The prices are fixed (downward

negotiable only) before the aircraft has been designed, 3 years before it will be flown and by contractors who have no experience with the extremely high tolerances required in the production of low observables. Production contract warranties require all OPEVAL – discovered specification deficiencies to be corrected at contractor expense although production on the first three contracts will be substantially complete before the conclusion of OPEVAL. Based on the above observations, I cannot unconditionally recommend that there is an "equitable and sensible allocation" of program risk between the contracting parties on the ATA program.

With respect to the second determination you are required to make, the Navy believes that the selected team of General Dynamics and McDonnell can absorb any losses though there has not been an economic analysis of either contractor's capacity to absorb a loss. The Navy does not believe there will be a major loss.

Attached are the questions I asked and the Navy's responses. Their earlier responses give rise to the concerns I've expressed.

/s/ Eleanor Spector
Eleanor Spector
Deputy Assistant Secretary
of Defense (Procurement)

Attachment

N00019-88-C-0050

FULL SCALE ENGINEERING DEVELOPMENT

N00019-88-C-0050

FOR

ADVANCED TACTICAL AIRCRAFT (ATA)

201/BRR/1105-87
Page 1 of 338 Pages

Copy: Cy206E-6

AWARD/CONTRACT [redacted] DO- A1

N00019-88-C-0050 201/BRR/0005-86

DEPARTMENT OF THE NAVY
Naval Air Systems Command
Washington, D.C. 20361
AIR-214K Ms B. Jones
Telephone: Area Code 202, 692-2020

See Section G

[redacted]

Pre-Award Survey Serial No.

McDonnell Douglas/McDonnell Aircraft Company/
General Dynamics/Ft Worth Division
P.O. Box 748
Ft Worth, TX 76101

See Section G

See Section F

See Section G

AA 1781804,4RZ3 003 AAA82 0 000000 20 000000
928WX0101800 $766,000,000.00

ITEM NO	SUPPLIES/SERVICES	QUANTITY	UNIT	UNIT PRICE	AMOUNT
	See attached pages.				

TOTAL AMOUNT OF CONTRACT ▶ $4,379,219,

16. TABLE OF CONTENTS

SEC	DESCRIPTION	PAGES
	PART I - THE SCHEDULE	
X A	SOLICITATION/CONTRACT FORM	
X B	SUPPLIES OR SERVICES AND PRICES/COSTS	1-2
X C	DESCRIPTION/SPECS/WORK STATEMENT	3-1
X D	PACKAGING AND MARKING	3-1
X E	INSPECTION AND ACCEPTANCE	4-1
X F	DELIVERIES OR PERFORMANCE	5-1
X G	CONTRACT ADMINISTRATION DATA	6-1
X H	SPECIAL CONTRACT REQUIREMENTS	7-1
	PART II - CONTRACT CLAUSES	
X I	CONTRACT CLAUSES	8-1
	PART III - LIST OF DOCUMENTS, EXHIBITS AND OTHER ATTACH	
X J	LIST OF ATTACHMENTS	9-1
	PART IV - REPRESENTATIONS AND INSTRUCTIONS	
K	REPRESENTATIONS, CERTIFICATIONS AND OTHER STATEMENTS OF OFFERORS	
L	INSTRS., CONDS. AND NOTICES TO OFFERORS	
M	EVALUATION FACTORS FOR AWARD	

CONTRACTING OFFICER WILL COMPLETE ITEM 17 OR 18 AS APPLICABLE

17. X CONTRACTOR'S NEGOTIATED AGREEMENT (Contractor is required to sign this document and return 1 copies to issuing office.) Contractor agrees to furnish and deliver all items or perform all the services set forth or otherwise identified above and on any continuation sheets for the consideration stated herein. The rights and obligations of the parties to this contract shall be subject to and governed by the following documents: (a) this award/contract, (b) the solicitation, if any, and (c) such provisions, representations, certifications, and specifications, as are attached or incorporated by reference herein. (Attachments are listed herein.)

18. ___ AWARD (Contractor is not required to sign this document.) Your offer on Solicitation Number ___ including the additions or changes made by you which additions or changes are set forth in full above, is hereby accepted as to the items listed above and on any continuation sheets. This award consummates the contract which consists of the following documents: (a) the Government's solicitation and your offer, and (b) this award/contract. No further contractual document is necessary.

19A. NAME AND TITLE OF SIGNER (Type or print)
Charles A. Anderson Vice Pres & General Mgr
W. S. Ross President

19B. NAME OF CONTRACTOR
BY W S Ross
19C. DATE SIGNED 5 Jan 88

20A. NAME OF CONTRACTING OFFICER
Bonnie L. Jones

20B. UNITED STATES OF AMERICA
BY Bonnie L. Jones
20C. DATE SIGNED 13JAN88

[redacted] APP. 19.315 201/BRR/1105-87

48

BEST AVAILABLE COPY

SCHEDULE

SECTION B - SUPPLIES OR SERVICES

Item	Supplies or Services	Quantity	Unit Price	Total Price
0001	ATA Aircraft Initial Design Review (IDR)	xxxx	xxxx	$244,150,654
0002	ATA Aircraft Preliminary Design Review (PDR)	xxxx	xxxx	$236,957,522
0003	ATA Aircraft Critical Design Review (CDR)	xxxx	xxxx	$504,160,441
0004	Data for Items 0001, 0002, 0003, 0049 and 0050			NSP (See Exhibit A and applicable Exhibit B Data Items)
0005	ATA Aircraft	8	xxxx	xxxx
0005AA	Same as Item 0005	1	xxxx	$209,006,809
0005AB	Same as Item 0005	7	$ *	$589,737,050
0006	Special Tooling and Special Test Equipment for Items 0001	xxxx	xxxx	$354,478,268

	through 0005 and 0049 and 0050			
0007	DELETED			
0008	Data for Items 0005, 0006 and 0051 through 0056			NSP (See Exhibit B)
0009	DELETED			
0010	Data for Items 0051 through 0056	xxxx	xxxx	NSP (See Exhibit C)
0011	Project Management	xxxx	xxxx	NSP

*$84,248,150

* * * *

0044	Data for Item 0043	xxxx	xxxx	NSP (See Exhibit U)
0045	Installation and Maintenance of High Response 40 Probe Inlet Distortion Rakes For Inlet Compatibility Measurements	(1) Set of 2 rakes Rt & Left Inlet	xxxx	NSP
0046	Data for Item 0045	xxxx	xxxx	NSP (See Exhibit V)

0047	CALS Technical Manual Program	xxxx	xxxx	$645,640
0048	Data for Item 0047	xxxx	xxxx	NSP (See Exhibit W)
0049	ATA Aircraft Program Management Review (PMR)	xxxx	xxxx	$286,214,572
0050	ATA Aircraft Program Management Review (PMR)	xxxx	xxxx	$182,325,015
0051	Phase I Test	xxxx	xxxx	$427,683,277
0052	Phase II Test	xxxx	xxxx	$308,653,614
0053	Phase III Test	xxxx	xxxx	$202,462,819
0054	Phase IV Test	xxxx	xxxx	$100,175,645
0055	Phase V Test	xxxx	xxxx	$76,708,495
0056	Phase VI Test	xxxx	xxxx	$514,271,392
0057	Training Equipment for Item 0005	xxxx	xxxx	$53,422,845
0058	Interim Contractor Logistics Support (ICLS) for Item 0057	xxxx	xxxx	$9,638,166

Total Target price	$4,379,219,436

*The prices shown above are the target prices. The corresponding target cost and target profit for each item is as follows.

Item	Target Cost	Target Profit
0001	$221,955,140	$22,195,514
0002	$215,415,929	21,541,593
0003	458,327,674	45,832,767
0005	726,130,782	72,613,077
0006	322,252,971	32,225,297
0022	71,388.374	7,138,838
0047	586,945	58,695
0049	260,195,065	26,019,507
0050	165,750,014	16,575,001
0051	388,802,979	38,880,298
0052	280,594,195	28,059,419
0053	184,057,108	18,405,711
0054	91,068,768	9,106,877

0055	69,734,995	6,973,500
0056	467,519,447	46,751,945
0057	48,566,223	4,856,622
0058	8,761,969	876,197
Total	$3,981,108,578	$398,110,858

The total price applicable to each item has been computed by adding to the target cost for such Item, the corresponding target profit set forth above for such item.

SCHEDULE

SECTION C - DESCRIPTION OR SPECIFICATIONS OR WORK STATEMENT

Item 0001 Initial Design Review (IDR)

The IDR shall be held at the contractor's plant, or at other locations as he may designate, to determine that the selected aircraft design approach is compatible with the engineering requirements of the contract. The IDR shall be held within four months after contract award to clarify and resolve potential areas of misunderstanding, and is a means of determining that the contractor has correctly understood all aircraft design & test requirements. The IDR shall be scheduled to be completed in one session of approximately five working days.

Item 0002 Preliminary Design Review (PDR)

The PDR shall be held at the contractor's plant, or at other locations as may be mutually agreed, to evaluate the progress, technical adequacy, and risk resolution (on a technical, cost and schedule basis of the selected design approach and determine its compatibility with performance and engineering requirements of the development specifications. The PDR will be scheduled in more than one session consistent with the completion schedule for the individual preliminary design efforts. The length of each individual review session shall be approximately four working days. At the conclusion of the incremental PDR's, a final PDR of approximately four working days will be held to

summarize the results of the individual PDR's. Completion and approval by NAVAIR (AIR 05) of the final PDR will result in authorization for the Contractor to proceed with the design of the ATA.

Item 0003 Critical Design Review (CDR)

The CDR shall be held at the contractor's plant or at other locations as he may designate to determine the potential of the detailed design of the ATA to satisfy the performance and engineering requirements of the ATA development specifications. The review shall be conducted when detail design and analysis is essentially complete (90%). The CDR will be scheduled in more than one session consistent with the completion schedule for the individual design efforts. The length of each critical individual review session shall be approximately four working days. At the conclusion of the incremental CDR's a final CDR of approximately four working days will be held to summarize the results of the individual CDR's. Completion and approval by NAVAIR (AIR 05) of the final CDR will result in authorization for the Contractor to proceed with the design of the ATA aircraft. The contractor shall furnish at CDR the information set out in Clause "Establishment of Not-to-Exceed prices for Option IV Items".

REDACTED Item 0005 - The contractor shall design, develop, manufacture and furnish eight (8) Full Scale Engineering Development (FSED) aircraft and associated mockups, models, and test articles in accordance with the Detail Specification for ATA Aircraft Weapon System, SD-574-1, including all Appendices.

Avionics Integration Laboratories shall also be developed as needed to provide a technically acceptable product within schedule constraints.

REDACTED The contractor shall (1) design ATA aircraft including the F404-GE-F502 engine through IDR, PDR and CDR in accordance with Detail Specification, SD-574-1, including all Appendices under Items 0001, 0002, 0003, 0049, and 0050 and (2) shall continue and complete the design of ATA aircraft including the F404-GE-F502 engine in accordance with Detail Specification, SD-574-1, including all Appendices under Item 0005 to include the design and development, fabrication and tests necessary to:

(1) **REDACTED** Cause the aircraft, engine and all other subsystems to conform to applicable specifications required by this contract.

(2) **REDACTED** Develop and qualify the F404-GE-F5D2 engine for incorporation into the ATA aircraft weapon system.

(U) The aircraft to be furnished hereunder shall be configured with the test instrumentation required for tests and demonstrations to be conducted in accordance with the requirements of 0051 through 0056. Test articles shall comply with the requirements of Detail Specification SD-574-1 and Addendum 648 to SD-8706C. The aircraft provided hereunder are assigned BUNOs, xxxxx0 thru xxxxx7.

(U) The contractor assumes the responsibility for integrating and interfacing any Government Furnished Equipment (GFE).

REDACTED The aircraft shall be equipped with the F404-GE-F5D2 engines developed in accordance with this contract. The contractor shall perform all work necessary to integrate the engine into the ATA aircraft and cause each to conform to applicable specifications required by this contract. The contractor shall perform all work necessary to qualify the engine to:

1. **REDACTED** Complete Prototype Preliminary Flight Qualification (PPFQ), Preliminary Flight Qualification (PFQ), Limited Production Qualification (LPQ) and Full Production Qualification (FPQ) in accordance with the requirements of Appendix E, Engine Model Specification, to Detail Specification SD-574-1.

A. (U) PPFO shall be considered complete upon:

(1) (U) Satisfactory completion of all the tests, inspections and analysis required by Appendix E, Engine Model Specification, to Detail Specification SD-574-1.

(2) (U) Government approval of all reports documenting the results of the above tests, inspections and analysis.

(3) (U) Satisfactory Contractor completion of corrective actions required to remedy any safety of flight related items revealed during development and testing of the engine.

(4) (U) Submittal and approval of corrective action plans to remedy any engine specification non-conformance revealed during development and testing of the engine.

(5) (U) Completion of at least 2100 total hours of full scale engine running time prior to the start of PPFQ endurance test.

B. (U) PFQ shall be considered complete upon

(1). **REDACTED** Satisfactory completion of all the tests, inspections and analysis required by Appendix E, Engine Model Specification, to the ATA Detail Specification, SD-574-1.

(2). (U) Government approval of all reports documenting the results of the above test, inspections and analysis.

(3). (U) Satisfactory Contractor completion of corrective actions required by either party to remedy any safety related nonconformance revealed during development and testing of the engine.

(4). (U) Submittal and approval of corrective action plans to remedy any engine specification nonconformances revealed during development and testing of the engine.

(5). (U) Completion of at least 3500 total hours of full scale engine running time prior to the start of PFQ endurance test.

C. (U) LPQ shall be considered complete upon:

(1) **REDACTED** Satisfactory completion of all the tests, inspections and analyses required by Appendix E, Engine Model Specification, to Detail Specification SD-574-1.

(2). (U) Government approval of all reports documenting the results of the above tests, inspections and analyses.

(3). (U) Submittal and approval of corrective action plans to remedy any engine specification nonconformances revealed during development and testing of the engine and full scale development testing of the aircraft.

(4). (U) Completion of at least 4600 total hours of full scale engine running time on a minimum of 6 in-house test engines prior to the start of LPQ endurance test.

D. (U) FPQ shall be considered complete upon:

(1). (U) Notwithstanding inspection and acceptance of aircraft containing engines hereunder, the Contractor shall perform corrective actions required to remedy any engine specification nonconformance revealed by development and testing of the engine and full scale development flight testing of the aircraft.

(2). **REDACTED** Satisfactory completion of all PFQ and LPQ requirements stated above.

(3). (U) Satisfactory completion of an additional 1000 hours Accelerated Simulated Mission Endurance Test (ASMET) conducted (1) in

accordance with paragraph 4.6.1.2 of the engine model specification, and (2) on the same nameplate engine used for the official LPQ ASMET with changes only as necessary to perform routine maintenance or update to the FPQ configuration.

(4). (U) Satisfactory completion of an altitude performance and operability demonstration conducted in accordance with paragraph 4.6.3 of the engine model specification on an engine conforming to the FPQ parts list.

(5). (U) Test verification (component and/or engine) to 90% confidence of the minus three sigma low cycle fatigue life or damage tolerance inspection interval for each critical rotation component and pressure vessel.

(6) (U) Accumulation of at least 9535 hours of full scale engine running time.

2. (U) Perform the work specified below. The following tasks shall be completed as a part of the engine qualifications and integration of the engine into the air vehicle:

(U) Task A -- The Contractor shall provide engineering and material support at all Government test facilities where the contractor proposes or requires testing. The Contractor shall provide depot and intermediate maintenance support for all engines and exhaust systems being tested at the government designated test facilities and the contractor's facility as well as provide organization maintenance

* * * *

SCHEDULE

Final Assembly for Option Item 0301 aircraft. and Second-Sourcing and Co-Production for the fifth lot of production aircraft.

REDACTED Item 0006 - The Contractor shall provide special tooling and test equipment required hereunder, and it shall be of a type, quantity and quality suitable for sustaining all applicable requirements of the ATA Program under Items 0001 through 0005 and 0049 and 0050.

REDACTED Item 0011 - The Contractor shall establish and maintain management activities in accordance with the Project Management Requirements for the ATA Aircraft Weapon System to satisfactorily complete the tests required by this contract. The program management effort shall be established with authority delegated at appropriate levels. Individual assignments within the management organization shall facilitate single-points-of-contact for interface with Government Managers in a timely manner. The Contractor shall commit such resources as are necessary to accomplish the requirement stated herein. Program Management shall be accomplished in accordance with Attachment 24, the Program Management Requirements for the ATA Aircraft Weapon System, as revised and updated for FSD, SD-574-1, Addendum 648 to SD-8706C, Addendum 116 to MIL-D-8708B(AS), ILS-DS-30A-155 and Attachment 25.

REDACTED The contractor shall participate in joint Navy/Contractor program level conference and reviews as follows:

A. **REDACTED** Program Reviews

Program Reviews shall be reviews of the current status of the contractor's overall ATA development program, and shall cover all principal technical, programmatic and contractual matters. Program Reviews will be held quarterly through CDR and then three times a year thereafter, at the prime contractor's plant and each normally will be three days in length. The agenda for each Program Review will be jointly established by the prime contractor and PMA-235. The first Program Review will be held within six months after contract award.

B. **REDACTED** Post Award Orientation

Post Award Orientation Conferences of the ATA shall be conducted at the prime contractor's plant to clarify procedural and administrative requirements and resolve potential areas of misunderstanding. The length of the conference shall be approximately two working days. The first post award orientation conference shall be held within 45 days after contract award.

* * * *

(U) Item 0045 - The Contractor shall design, develop, install and maintain one set (left and right hand inlet) of high response inlet distortion rakes for one aircraft in order to validate and develop, if necessary, engine/inlet compatibility. Rakes shall be designed in accordance with Appendix E of the Detail Specification, SD-574-1.

(U) Item 0047 - The Contractor shall establish and provide a CALS Technical Manual Program for Item 0005, in accordance with ILS-DS-30A-155, Chapter 1, paragraphs 1.3.10 and 1.3.10.1.

REDACTED Item 0049 - The Program Management Review (PMR) shall be held at the Contractor's plant and shall review the current status of the overall ATA development program, addressing all principal technical, programmatic and contractual matters. This PMR shall not be considered complete until the Contractor provides the following top level principal system installation drawings and top level major component structural assembly drawings evidencing 100% drawing release:

Systems:

(u) Fuel Subsystem
(u) Electrical Subsystems
(u) Environmental Control System
(u) Hydraulic/Pneumatic Subsystem

Structural Assemblies:

(u) Forward Fuselage
(u) Centerbody
(u) Outboard Centerbody
(u) Aft Section
(u) Outer Wing

REDACTED Item 0050 - The Program Management Review (PMR) shall be held at the Contractor's plant and shall review the current status of the overall ATA development program, addressing all principal technical, programmatic and contractual matters. This PMR shall not be complete until the following items are also completed:

(u) Software CDR, Build #3, as defined in Paragraph 5.3.3 of MIL-STD-2167.
(u) Detailed design and analysis of FSD "0" Level Hydro-mechanical support equipment essentially complete (90%).
(u) IAFTA core hardware and software design for the initial six (6) WRA's.

REDACTED Item 0051 - The Contractor shall perform Phase I of ATA design examinations, tests and engineering to substantiate, assess and/or effect compliance with design requirements in accordance with Addendum 648 to SD-8706C. The Contractor shall provide test articles, test hardware, hardware support and test planning and shall conduct the portion of testing in accordance with Addendum 648 to SD-8706C required to conduct the Critical Design Review (CDR). This includes the

initial effort required to design and fabricate a full size aircraft and cockpit mock-ups that will satisfy the requirements for aircraft, lighting and aircrew station mock-ups as specific in paragraph 3.3.2 of Addendum 658 to SD-8706C. In addition, the Contractor shall perform Phase I of ATA aircraft demonstrations in accordance with Addendum 116 to MIL-D-8708B (AS).

REDACTED Item 0052 - The Contractor shall conduct Phase II of testing in accordance with Addendum 648 to SD-8706C and Addendum 116 to MIL-D-8708B(AS) as required to effect the first flight of the first ATA aircraft. The following tests shall be completed:

(u) First major static condition
(u) Fatigue/Static Strength Pitch Flap
(u) Propulsion PPFQ
(u) Proof Test Control Surfaces on Aircraft #1
(u) Crew Escape - Sled tests
(u) Canopy Pressure tests
(u) Cockpit controls/maximum pilot effort
(u) Iron Bird Hydraulic System Functional
(u) Static Strength MLG & NLG

REDACTED Item 0053 - The Contractor shall conduct Phase III of testing in accordance with Addendum 648 to SD-8706C and Addendum 116 to MIL-D-8708B(AS) as required for the Navy to

commence Sea Trials. Aircraft of Item 0005 and certain production aircraft specified in Clause H-28 hereof shall be used for tests and demonstrations in accordance with Addendum 116 to MIL-D-8708B(AS). The following tests shall be completed:

(u) Bird strike tests
(u) Propulsion PFQ
(u) Clean aircraft drop tests
(u) 1G envelope (clean aircraft)
(u) RCS Baseline static measurement
(u) Emergency recovery device proof test - Aircraft #8
(u) Closed loop/degraded modes (iron bird)

REDACTED Item 0054 - The Contractor shall conduct Phase IV of testing in accordance with Addendum 648 to SD-8706C and Addendum 116 to MIL-D-8708B(AS) as required through provisional acceptance of the fourth production aircraft to be used for tests and demonstrations in accordance with Addendum 116 to MIL-D-8708B(AS). Aircraft of Item 0005 and certain production aircraft specified in Clause H-28 hereof shall be used for tests and demonstrations in accordance with Addendum 116 to MIL-D-8708B(AS). The following tests shall be completed:

(u) Flight tests 100% loads
(u) Second Dynamic RCS measurement
(u) Fatigue test - 2 lifetimes

(u) CBR intrusion test
(u) Drop tests Deck Obstruction Test

REDACTED Item 0055 - The Contractor shall conduct Phase V of testing in accordance with Addendum 648 to SD-8706C and Addendum 116 to MIL-D-8708B(AS) as required to deliver the first ATA aircraft to the Navy for commencement of TECHEVAL. Aircraft of Item 0005 and certain production aircraft specified in Clause H-28 hereof shall be used for tests and demonstrations in accordance with Addendum 116 to MIL-D-8708B(AS). The following tests shall be completed:

(u) Propulsion LPQ
(u) Repeated fatigue drops
(u) Fuel ingestion
(u) Laboratory armament tests
(u) RCS airframe RAMS Spec test
(u) Third Dynamic RCS measurement

REDACTED Item 0056 - The Contractor shall conduct Phase VI of testing in accordance with Addendum 648 to SD-8706C and Addendum 116 to MIL-D-8708B(AS) as required to the completion of TECHEVAL on all TECHEVAL aircraft. Aircraft of Item 0005 and certain production aircraft specified in Clause H-28 hereof shall be used for tests and demonstrations in accordance with Addendum 116 to

MIL-D-8708B(AS). The following tests shall be completed:

(u) Flight Control System Integration (iron bird)
(u) Aircraft No. 2 propulsion tests
(u) Contractor flight tests
(u) Structural Dynamic Service Life Effects
(u) Aircraft High Angle of Attack

REDACTED Item 0057 - The Contractor shall furnish Aircrew Training Devices for Item 0005 in accordance with Appendix C, (Appendix E) to ILS-DS-30A-155, the Training System Specification, Chapters 3.0 - 5.0, paragraphs 3.2, 4.2 and 5.2.

REDACTED The Contractor shall also furnish a suite of Maintenance Training devices in accordance with Appendix C (Appendix F) to ILS-DS-30A-155, the Training System Specification, Chapters 3.0 - 5.0, paragraphs 3.3, 4.3 and 5.3.

REDACTED The Contractor shall continue to establish and conduct the Aircrew and Maintenance Training Curricula, Design, Development and Implementation programs and Evaluation, Maintenance and Revision Programs defined in Item 0022.

REDACTED Item 0058 - The Contractor shall perform Interim Contractor Logistics Support (ICLS) for Item 0057 in accordance with paragraph

1.2.2 of Appendices C and D to Appendix C of ILS-DS-30A-155.

REDACTED Option Items 0101, 0201, 0301, 0401. The Contractor shall fabricate, assemble and delivery ATA aircraft in accordance with SD-574-1 and Appendices thereto. Sustaining Tooling Support for Production, such as the costs of maintenance and refurbishment due to normal wear and tear, methods improvements, quality assurance and calibration, subcontractor production non-recurring, establishment of dual final assembly and co-production capability , and establishment and qualification of vendor second sources shall be included in the respective option prices. For Option Item 0101 the contractor shall implement the process described in the clause entitled "Dual Sourcing and Co-Production Capability". Under Option Item 0101, the avionics system shall be tested in accordance with paragraphs 4.1, 4.3, 4.4 and 4.5 of Appendix D to Detail Specification, SD-574-1. Under Option Items 0201 and 0301 the avionics systems shall be tested in accordance with paragraphs 4.1, 4.4 and 4.5 of Appendix D to Detail Specification, SD-574-1. Under Option Item 0401 the avionics system shall be tested in accordance with paragraphs 4.1, 4.4 and 4.5 of Appendix D to Detail Specification, SD-574-1, for all CI's and paragraphs 4.3 and 4.5 (equivalent) of Appendix D to Detail Specification, SD-574-1, for second-sourced CI's.

REDACTED Production aircraft shall have the following alternate mission equipment attached at delivery.

Per Aircraft Qty	
6	BRU-32/A Bomb Rack
4	ALE-39 Chaff Dispenser
1	Fuel Probe (IFR) Tip
2 sets	Survival Kit Components
1	Radar Altimeter
1	X-Band Beacon
2	LAU-127 Missile Launcher
6	Tandem Adapter
12	DAC 4010 Rack

REDACTED The following alternate mission equipment shall be shipped separately:

Qty	Per Aircraft	
1	1	BRU-32/A Bomb Rack
1	1	Chal Adapter
1	1	Lode 14 Rack

1	4	Primary Auxiliary Fuel Tank
1	4	Secondary Auxiliary Fuel Tank
1	12	Mod 28-200 Refuel Store
1	12	D-704 (or equivalent Refuel Store)
1	1	External Pylon
1	1	400 Gallon Tank
1	2	BRU-41 Rack
1	2	BRU-42 Rack
12	10	LAU-117 Missile Launcher
2	5	Lau-115 Missile Launcher

REDACTED The engines delivered integrated with the ATA aircraft hereunder shall conform to both (a) the requirements of Engine model Specification Appendix E to SD-574-1 and b) the drawings depicting the parts comprising the parts list as modified by Class I and Class II changes for the engine configuration which successfully

completes Limited Production Qualification (LPQ) or Full model specification noncompliance found during flight tests. If the obligation to conform to any such drawing conflicts with the obligation to conform to the specification requirements, the specification requirements shall prevail; however, a part appearing on such parts list may not be changed in any manner from the version depicted on its applicable drawings in order to conform to specification requirements unless the change is approved under the Configuration Control Procedure described in special provision H-36.

(U) The engines shall be acceptance tested in accordance with the engine model specification Appendix E to SD-574-1.

(U) The contractor shall maintain a quality assurance program in accordance with MIL-Q-9858A, Amendment 2. Additionally the contractor shall provide and maintain a corrective action and disposition system for nonconforming material in accordance with MIL-STD-1520A with Notice 1 and a supplier quality assurance program in accordance with MIL-STD-1535A for all supplies and services provided under this contract.

SCHEDULE

H-1 SPECIAL SECURITY REQUIREMENTS FOR COMPARTMENTED CONTRACTS

1. **[REDACTED]** GENERAL. This contract pertains to a program, part of which is compartmented, and which contains Sensitive Compartmented Information (SCI) and Special Access Program (SAP) information. Access to SCI and SAP information under this contract is limited to those personnel who have been properly briefed in accordance with the Program Security Manual (PSM) and have executed a Program Indoctrination Agreement. The contractor shall provide and maintain a secure control system within an approved program facility in accordance with the requirements and restrictions of (1) this clause; (2) the Program Security Manual (PSM); (3) attachment 34, Contract Security Classification Specification (DD-254) and attachment thereto; and (4) attachment 45; Security Implementation Plan. Clarification of security requirements and restrictions will be provided upon request by the Program Security Officer (PSO).

2. **[REDACTED]** PROGRAM SECURITY OFFICER/ASSISTANT PROGRAM SECURITY OFFICERS. **[REDACTED]** responsibility has been assigned to the PSO, NAVAL AIR SYSTEMS

COMMAND (NAVAIRSYSCOM). The PSO is the US Navy official responsible for all aspects of security for the BRAVERY program. The PSO is aided by Assistant Program Security Officers (APSO), who will enforce the security policies and procedures of the program.

3. (U) PROGRAM SECURITY COORDINATOR. The Contractor shall designate with the approval of the PSO, a Program Security Coordinator (PSC) who, assisted by a staff assigned for these functions, shall be assigned the responsibility for assuring compliance with the provisions of this CLAUSE, the DD 254, and the PSM made a part of this contract by reference, and with any clarification of security requirements and restrictions provided by the PSO.

4. (U) SECURITY VIOLATIONS. Security is a material part of this contract. A violation of any of the requirements and restrictions of this clause, and of any PSM which may be incorporated by reference in this contract, may result in debriefing and removal from access to the classified/compartmented portion of the program, and may also be grounds for termination of the contract for default. Further, any unauthorized disclosure of the classified information pertaining to this contract or program could seriously affect the national defense of the United States, and such revelation would be subject to federal prosecution under the Espionage Laws (Title

18, United States Code, Section 793, 794 and 798).

5. **[REDACTED]** CONTRACTOR PROGRAM FACILITY. The PSO shall, with PSC, inspect the contractor's facility to ensure compliance, storage capability, and adequate safeguarding of all program material. Under no circumstances will storage of, or work on compartmented program material be performed in other than the approved program facility.

6. (U) PUBLIC DISCLOSURE. Public disclosure or conformation of any subject matter relative to this contract is not authorized without first obtaining written approval from the PSO and the PCO.

7. (U) INVOICE/VOUCHER SUBMISSION. See Section G.

8. **[REDACTED]** DD 254. The DD 254 and the contract number for the BRAVERY program are unclassified and may be shown to DEFINVSERV inspectors when requested, but inspectors are not to be allowed access to the contract or the BRAVERY program facility. If they insist, the DEFINVSERV inspectors are to be told to contact **[REDACTED]** PSO, on (202) 692-2020. The PSO shall also be notified immediately by telephone, in order that appropriate action can be taken.

7. (U) WAIVER OF CONTRACT OR SECURITY REQUIREMENTS. Any conflict which may exist between this clause and the PSM or instructions from the PSO or PCO shall immediately be brought to the attention of the PCO. Resolution shall be authorized by the PCO in writing.

8. (U) CORRESPONDENCE. Mailing of correspondence will be in accordance with the guidance contained in attachment 45, Security Implementation Plan.

H-2 (U) CERTIFICATION OF INDIRECT COSTS (APR 1986) (DOD FAR SUP 52.242-7003)

(a) (U) The Contractor shall certify any proposal to establish or modify billing rates or to establish final indirect costs rates in the form set forth in paragraph (b) of this clause. The certificate shall be signed on behalf of the Contractor by an individual of the Contractor's organization at a level no lower than a vice president or chief financial offer of the business segment of the Contractor that submits the proposal. The Contractor understands that if the Contractor fails to submit a certificate as required herein, payments on account of indirect cost shall be at rates unilaterally established by the Government.

SCHEDULE

H-7 (U) ALLOTMENT OF FUNDS APPLICABLE TO FSED ITEMS

(a) (U) The supplies and services to be furnished under the basic contract FSED Items shall be funded by the Government on an installment basis. This financing arrangement is necessitated by the unavailability for obligation, at the outset of this contract, of sufficient funds to cover the total target values or ceiling price of the basic FSED contract line items.

(b) (U) The Contractor agrees that the Government's obligation of funds in the amounts and by the dates set forth below will permit compliance with the contract. The Contractor acknowledges that the terms and conditions for the performance of this contract have been established on the basis that the Contractor's termination liability will not exceed the amount set forth below by the dates set forth opposite said amounts. Nothing herein shall authorize nor require the Contractor to incur costs, plus a reasonable allowance for profit, in excess of the total amount obligated at any given time. The Contractor may request the Government, but the Government shall

not be obligated, to provide funds at a more rapid rate than described herein. The Contractor shall not be entitled to reimbursement of costs incurred by the Contractor through progress payments when the Contractor exceeds the amount of obligation specified herein. However, when amounts are obligated, any costs incurred by the Contractor prior to such obligation shall be allowable to the same extent as if such costs had been incurred after such amounts had been obligated.

REDACTED

Installment	Date by Which Installment Will be Obligated	Amt. of Obligation (Not cumulative)
1	Date of Contract	$150,000,000.00
2	14 Jan 1988	$616,000,000.00
3	01 Nov 1988	$286,000,000.00
4	07 Jan 1989	$861,300,000.00
5	01 Nov 1989	$350,000,000.00
6	07 Jan 1990	$1,050,000,000.00

7	01 Nov 1990	$185,000,000.00
8	07 Jan 1991	$553,200,000.00
9	01 Nov 1991	$55,900,000.00
10	07 Jan 1992	$167,600,000.00
11	01 Nov 1992	$104,219,436.00

(c) (U) In the event the Government fails to obligate any specified installment by the time specified, the Contractor will continue performance of the contract only to the extent that he shall not be required to incur obligations (termination liability) beyond that amount already obligated by the Government. If the Government fails to obligate any funds at the time specified and there are not previously obligated funds remaining, the Contractor shall notify the Contracting Officer. After receipt of this notification, the Contracting Officer has thirty (30) days to provide additional funds or must issue a stop work order not to exceed a period of thirty (30) days. If the Contracting Officer issues a stop work order and then funds the contract during the work stop period, the target values and ceiling price, delivery schedules, and terms and

conditions of this contract shall be equitably adjusted, to the extent that it can be demonstrated by the Contractor that such failure to obligate funds affected contract cost and/or performance. The Government's total obligation for payment (including termination settlement expenses) under this contract shall not exceed the total amount obligated at the time of termination.

(d) (U) Change Orders issued pursuant to the "Changes" clause of the contract shall set forth funds estimated at the time to be sufficient to perform the change unless otherwise agreed to by the parties. Pending any equitable adjustment pursuant to said clause, the funds set forth in the change order shall be added to the then established amount of installment funds set forth in paragraph (b) above.

(e) (U) Nothing contained in this clause shall affect the right of the Government to terminate this contract pursuant to either the "Default" or "Termination for the Convenience of the Government" clauses.

(f) (U) The Government may obligate funds at a more rapid rate than set forth above without affecting any other term or condition of this contract.

(g) (U) If Congress appropriates funds which require incremental funding for all or any party of Option I, a clause similar to this "Allotment of Funds" clause will apply to that incremental funding portion of Option I.

(END OF CLAUSE)

electronic systems with advanced technology, and provide maximum commonality with the Advanced Tactical Fighter (ATF) program. Therefore, any features in accordance with the Joint Integrated Avionics Working Group (JIAWIG) common avionics baseline (CAB-1) definitions that can be incorporated in the baseline design to ease or make less expensive the transition during P3I should be emphasized. The CAB-1 documents are available separately from the Program Office.

(END OF CLAUSE)

H-28 **(REDACTED)** Government Property for the Performance of this Contract (Fixed-Price) (Apr 1985) (NAVAIR 52.245-9500)

(a) (U) Definition. Government production and research property, as the term is used herein, shall consist of special tooling to which the Government has title or the right to acquire title, Government-owned special test equipment and Government-owned facilities as each term is defined respectively in FAR 45.101 and 45.301.

(b) (U) Authorization to Use Government Production and Research Property, Material, and Agency Peculiar Property Currently Covered by Government Contracts Without Rental Charge in Performing this Contract. Government production and research property, material, and agency peculiar property covered by the following listed Government contracts on the effective date of this contract is hereby authorized for use on a rent-free, non-interference basis in the performance of this contract and sub-contracts of any tier issued hereunder (except for Items identified as Foreign Military Sales (FMS) Items in Section B):

(b)(1) **(REDACTED)** For McDonnell Aircraft Company and Subcontractors

F33657-76-A-0053
F33657-77-C-0027
F33657-78-C-0513
F33657-82-C-0067
F42600-80-C-5225
F42600-81-C-5482
F42600-82-D-4980
F42600-83-C-4577
N00019-82-G-0101
N00383-75-A-6533
N00383-77-A-7500
N00383-78-A-8504
N00383-81-G-1500
N00383-83-G-3500
F33657-78-C-0645
N00383-84-G-4510
F09603-75-A-0164
F09603-76-A-1729
F09603-77-C-0743
F09603-78-G-1129
F09603-80-C-0229
F09603-80-C-1472
F09603-80-G-0001
F09603-80-G-0285
F09603-81-G-1045
F33615-79-C-3627
F33615-84-C-3015
F33657-76-C-0464
F33657-78-C-0527
F33657-78-G-0007

F33657-79-C-0779
F33657-80-C-0056
F33657-81-G-2168
F33657-81-G-2169
F33657-83-C-0043
F33657-83-C-2133
F33657-84-C-2002
F33657-84-C-2131
F33657-84-C-2228
F33657-85-C-2086
N00383-81-G-1500
N00383-83-G-3500
N00019-78-C-0526
N00019-80-C-0173
N00019-81-C-0157
N00019-81-G-0455
N00019-81-G-0509
N00019-82-C-0440
N00019-82-C-0501
N00019-82-G-0475
N00019-83-C-0272
N00019-83-C-0335
N00019-83-C-0336
N00019-83-C-0431
N00019-83-G-0277
N00019-83-G-0412
N00019-84-C-0063
N00019-84-C-0116
N00019-84-C-0200
N00019-84-C-0270
N00019-84-H-0418
N00019-85-C-0002
N00019-85-C-0003
N00019-85-G-0076
N00019-85-G-5300
N62269-84-C-0111
N00019-76-C-0666
N00019-79-C-0165
N00019-79-G-0008
N00019-80-C-0655
N00019-80-G-0101
N00019-81-C-0497
N00019-82-C-0359
N00019-82-G-0460
N00019-83-C-0119
N00019-83-C-0267
N00019-85-C-0109
N00383-84-G-4510
N61339-82-C-0022
F33615-78-C-3601
F33657-77-A-0001
N61339-76-C-0063

(U) McDonnell Aircraft and Subcontractor Facilities Contracts:

Vendor	Facility Contract No.	Exp. Date
Allied-Bendix Teterboro NJ	DAAH01-86-E-0001	0191
Brunswick Prod Marion VA	F33657-72-C-0078	0787
Cleveland Pn Co Cleveland OH	F33657-78-L-0113	1088
Cleveland Pn Co Tullahoma TN	N00019-84-E-9017	0290
GE Aircraft El Binghamton NY	F33657-80-E-0297	1288
GE Armament Sys Burlington VT	DAAA09-86-E-0007	0791
Hamilton-Sta Windsor Locks CT	N00019-86-E-9005	0991
Honeywell Ind St. Louis Pk MN	DAAA09-76-E-0030	0987
Honeywell Ind St. Louis Pk MN	N00024-82-E-5429	0788
Hughes Aircraft Culver City CA	DAAH01-86-E-A001	0591
Hughes Aircraft Culver City CA	N00030-85-E-0122	0290
Hughes Aircraft Culver City CA	NAS3-19569-F	0388
Hughes Aircraft Culver City CA	NAS5-26229	E
Hughes Aircraft Tucson AZ	F33657-81-E-2096	1187
Martin Marietta Orlando FL	DAAH01-85-E-A001	0390

Martin Marietta Orlando FL	F09306-83-C-3990	1290
MDAC Huntington Beach CA	NAS7-527F	1288
MDC St. Louis MO	N00019-83-E-9030	1090
MDC St. Louis MO	N00019-83-L-9032	0199
MDC Tulsa OK	F33657-72-L-0647	0290
Northrop Corp Hawthorne CA	N00030-85-E-0135	0590
Pacific Clark-Aiken El Segundo CA	F33657-81-E-2181	0887
Sanders Associates Manchester NH	N00019-84-E-9015	1289
Tico Titusville FL	DAAH01-74-C-2721	0789
World Aerospace Minneapolis MN	N00019-82-E-9013	0687

(b)(2) **(REDACTED)** For General Dynamics:

F61546-80-C-0014	F33657-83-C-0340
DAAH01-83-D-A006	F04606-78-C-0358
DAAH01-85-C-A050	F08635-82-C-0366
DAAH01-85-C-A095	F33657-81-C-0432
P0111-4927-A101	F04606-78-A-0541
F61546-83-C-0001	F33657-74-C-0591
F41606-83-A-0002	F33657-78-C-0669
F41608-76-A-0003	F04606-83-C-0795
F33657-78-G-0004	F33615-83-C-1029
DAAD07-85-C-0009	F04606-78-C-1042
F41608-86-D-0023	AF33657-13403
F41608-81-G-0024	F04606-82-C-1408
F41608-80-G-0028	NAS 3-16080F
F41608-78-G-0032	NAS 3-16090

F41608-84-G-0036
F41608-85-G-0044
F41608-81-G-0046
F19628-83-C-0054
F04606-84-D-0065
DSA500-77-A-0069
F04606-85-D-0073
F33657-82-D-0079
F26600-79-C-0098
F04606-80-C-0099
F08635-78-C-0103
F04606-80-D-0112
F04606-82-D-0125
F04606-83-C-0126
N00019-85-C-0146
F04606-82-C-0156
F41608-82-D-0157
F33657-80-D-0169
F33657-86-C-0171
F30602-83-C-0178
F33657-76-C-0191
F33657-84-C-0192
F33657-76-C-0197
F33657-80-L-0242
F33657-84-C-0247
F33657-84-C-0249
DAAK40-79-C-0263
F30602-80-C-0270
F33657-81-C-2012
F33657-82-C-2034
F33657-82-C-2038
F33657-82-G-2084
F33657-82-G-2085
F33657-82-C-2120
F33615-78-C-3022
F33615-83-C-3227
F33615-80-C-3239
F09603-83-D-3573
F41608-86-M-3846
F42600-83-D-4006
F42600-83-D-4008
F42600-83-C-4010
F42600-83-C-4011
F42600-84-C-4196
F42600-82-C-4580
F42600-85-D-4599
F42600-85-D-4600
F42600-85-D-4601
F42600-85-D-4910
F33615-83-C-5079
F33615-81-C-5122
F33615-73-C-5178
F42600-82-C-5730
F42600-82-C-7509
NAS 3-22337
F33657-75-C-0310

(REDACTED) General Dynamics Facilities Contract:

Contract No.	Exp. Date

(b)(3) **(REDACTED)** For McDonnell Aircraft and General Dynamics: Subject to the provisions of paragraphs b(1) and (2) above, any of the aforementioned items of special tooling and/or special test equipment presently in the possession of the Contractor and/or subcontractors may be modified as necessary for the performance of this contract subject to the approval of the requiring contract PCO. It is, however, hereby provided that such modification shall not interfere with the proper performance of work under the contract(s) for which they were originally produced, acquired or furnished and that the Contractor shall return the modified equipment to its original configuration after use. .

In addition, each Contractor may use, on a rent-free, non-interference basis, any of the other Contractor's Government-furnished property under this clause at the St. Louis, Missouri, Fort Worth Texas or Tulsa, Oklahoma locations.

(b)(4) **(REDACTED)** For General Electric:

Evandale:	F33657-73-L-0248
Lynn, Mass:	N00019-76-C-0261
	N00019-78-C-0063
	N00019-79-C-0152
	N00019-80-C-0021
	N00019-81-C-0050
	N00019-81-E-9003
	N00019-82-C-0042
	N00019-83-C-0086

N00019-83-C-0150
N00019-83-C-0156
N00019-84-C-0140
N00019-84-C-0136
N00019-84-C-0137
N00019-85-C-0129
N00019-85-C-0160
N00019-85-C-0162
N00019-86-C-0048
N00019-86-C-0195
N00019-86-C-0166
N00019-85-C-0459 and successor contracts

(REDACTED) For General Electric Subcontractors:

American Welding & Mfg. Co., Warren, OH	F33657-71-C-0122
Arkwin Industries Inc.	F33657-71-C-0625
Bendix Corp., Energy Controls Div.	F33657-79-C-0020
Chandler Evans Corp.	F33657-68-C-1332
King Fifth Wheel co.	F33657-70-C-0952
Reeder & Kline Machine	F33657-84-E-2157
TRW, Inc., Minerva OH	F33657-70-C-0272
Sundstrand	F33657-70-C-0819

(b)(5) (U) Consideration has been provided for all prime and subcontractor facilities usage, as identified above, on a rent-free, non-interference basis. However, notwithstanding paragraph (1) hereof, complete definition of Government production

and research property (in particular, facilities) cannot be determined until subcontracting decisions have been completed by the Contractor. It is understood and agreed that subcontractor determinations for facilities use on a rent-free, non-interference basis in the performance of this contract will be rendered on the premise that if such Government production and research property can be made available on a rent-free, non-interference basis, it will be identified and added to this section at the time of subcontract definitization without further consideration being required.

(c) (U) Authorization to Use Government Production and Research Property and Agency Peculiar Property to be Provided Under this Contract Without Rental Charge in Performing this Contract. (This paragraph does not cover such property in possession of the Contractor or his subcontractors on the date of award of this contract.)

(1) (U) Subject to the provisions of the Government Property clause of this contract, the Government hereby agrees to provide hereunder the Government production and research property and agency peculiar property identified in (c)(2) through (c)(5) to the Contractor. The Contractor is hereby authorized to use, on a rent-free basis, said property in the performance of this contract (except for Items identified as Foreign Military Sales (FMS) Items in Section B).

(2) (U) Special Tooling (as defined in FAR 45.101):

Special Tooling acquired under Item 0006 which may have been upgraded under Option Item 0102.

(3) (U) Special Test Equipment (as defined in FAR 45.101):

Special Test Equipment acquired under Item 0006 which may have upgraded under Option Item 0102.

(4) (U) Facilities (as defined in FAR 45.301):

NONE

(These facilities shall, when proven, become accountable under and be subject to that facilities contract, if any, in effect between the Government and the Contractor or any of his subcontractors at the plant where they are to be located during performance of this contract.)

(5) (U) Agency Peculiar Property (as defined in FAR 45.301 and DOD FAR (Supplement 45.301):

(a) **(REDACTED)**"For demonstrations under Items 0051 through 0056, 0203, 0332, and 0405, the Government will furnish: eight (8) ATA Aircraft, which have been provisionally accepted under Item 0005, to perform flight demonstrations; and four (4) ATA Aircraft

delivered under Item 0101 to perform production flight demonstrations. These aircraft shall be provided on the dates listed below:

	Aircraft Number	Need Date
Item 0005:	1	July 1990
	2	August 1990
	3	September 1990
	4	October 1990
	5	November 1990
	6	December 1990
	7	January 1991
	8	February 1991
Item 0101:	1	July 1991
	2	September 1991
	3	November 1991
	4	January 1992

For purpose of this paragraph (5)(a) and notwithstanding the provisions of FAR 52.245-2(a)(4), if the aircraft listed above are not delivered to the Contractor by the "need dates" listed above and such late delivery is attributable to the Contractor's delay in tendering the aircraft for acceptance as set out in Section F hereof, an equitable adjustment shall not be made.

(REDACTED) Spare, repair and/or replacement parts for the aircraft designated above and for support equipment may be drawn from current production assets (for replacement of assets removed from aircraft for repair, maintenance or testing

purposes) and returned on a "payback" basis (in the same conditions as furnished, normal wear and tear excepted, and in a timely manner). The Contractor may use GFP assets in conjunction with, or in place of, production assets when authorized by the PCO. If any of these production/GFP assets are used in the designated aircraft, the Contractor shall provide a brief written report stating parts employed, circumstances necessitating use, and the status of the "payback" part. This report shall be provided to the ACO, PMA, and PCO within two (2) weeks of the conclusion of demonstrations under Item 0051 through 0056 and 0203.

(b) (U) Aircrew protective and flight safety equipment as necessary to support production acceptance flights or test flights associated with the performance of this contract as itemized below:

Equipment	Qty per Pilot or B/N*	Total Estimated Qty for FSD including 10% spares
Oxygen mask & Regulator	1	26
Life Preserver Unit	1	26
Parachute Harness	1	26
Anti-g suit	1	26
Aviator's gloves	1 pr	26 pr
Helmet	1	26
Mask & attaching pieces	1	26

Boots	1 pr	26 pr
Flight suits	2	52
Exposure suits	1	26
Sunglasses	1 pr	26 pr
Socks	1 pr	26 pr

* Per pilot quantities will remain unchanged throughout the production program.

(c) (U) Chase and Target aircraft as required in performance of this contract as follows:

Location	Chase & Target A/C qtv	Requirement Dates
MDC Tulsa	2*	5/1990 throughout the program
NATC, Pax River	Average: 6** Peak: 8**	5/1990 - 1/1993
NWC, China Lake	2**	11/1990 - 6/1993

* To be maintained and operated by the Contractor; must be two seat configuration.

** To be maintained and operated by the Government.

(REDACTED) Definition of Chase and Target Aircraft: Aircraft can be subsonic, must be

compatible with the Model 21 in regard to endurance, and must have secure voice communication capability; target aircraft must include a minimum of one each F/A-18, A-4, A-7 and A-6.

(d) (U) All Support Equipment, Technical Data or other Equipment listed in Attachment 36 to this Contract.

(U) The following terms and conditions shall be applicable to the agency peculiar property, if any, identified above:

(A) (U) each item of agency peculiar property shall be identified by its Federal Item Identification number and Government Nomenclature;

(B) (U) the agency peculiar property shall be accounted for under this contract; and

(C) (U) upon completion or termination of this contract, the Contractor shall request and comply with disposition instructions from the Contracting Officer.

(d) (U) Government Material and Agency Peculiar Property to be Furnished Under this Contract. (This paragraph covers Government-owned material and agency peculiar property furnished to the Contractor for (A) consumption in the course of manufacture, testing, development, etc., or (B) incorporation in items to be delivered under this contract, e.g.,

Master Government-Furnished Equipment List (MGFEL)).

(1) (U) Subject to the provisions of the Government Property clause of this contract, the Government hereby agrees to provide hereunder the Government-owned agency peculiar Property and material identified in (d) (2) and (d) (3) to the Contractor. The Contractor is hereby authorized, as appropriate, (A) to consume the material identified in (d) (3) in performing this contract or (B) to incorporate such material and agency peculiar property in articles under this contract.

(2) (U) Material (as defined in FAR 45.301):

(a) **(REDACTED)** Fuel (Fleet Common) while ATA is being supported under this contract. See the clause entitled "Government Furnished Petroleum, Oil and Lubricants."

(b) (U) Material items identified in Appendix I to Detail Specification SD-574-1. Delivery dates to the Contractor shall be derived from the aircraft delivery schedule in Section F hereof, using Installation Lead Time (ILT) contained in the above identified document.

(U) Requisitioning Documentation. If material is identified above, the requisitioning documentation for the above material shall be prepared by the Contractor in accordance with the "Military Standard Requisitioning and Issue Procedure (MILSTRIP) for Defense Contractors", DOD FAR

Supplement Appendix H. Upon completion or termination of this contract, the Contractor shall request and comply with the disposition instructions from the Contracting Officer.

(3) (U) Agency Peculiar Property (as defined in FAR 45.301 and DOD FAR Supplement 45.301: NONE

(U) The terms and conditions made applicable to agency peculiar property in (c) (5) shall be applicable to the agency peculiar property, if any, identified above.

(e) (U) Government Installations to be Made Available Under this Contract. (This paragraph covers Government installations, or portions thereof, to be made available to a contractor but not transferred to his possession -- for example, test centers, wind tunnels, aircraft fields, as well as buildings, furniture, or equipment. Instructions may be needed to establish ground rules or plans governing availability of installations.)

(1) (U) The Government hereby agrees to make available hereunder on a rent-free, non-interference basis for performing the contract Items in Section B the Government installations, or portion thereof, identified in (e) (2) in accordance with standard operating procedures and priorities unless otherwise specified in the Schedule. Although not "Government-furnished property" under this contract, the provisions of paragraph (a) of the

Government Property clause of this contract shall apply to these installations.

(2) **(REDACTED)** Installations:

(a) **(REDACTED)** The Navel Air Test Center, NAS Patuxent River Maryland shall be the principal test site and the Naval Weapons Center, China Lake, California shall be the secondary test site for the ATA FSD Flight Test Program. The facilities and resources of the principal and secondary test sites (the host) shall be provided to the Contractor within the existing capabilities and resources available at the test sites during the FSD program. The responsibility to provide resources beyond those specified herein shall be borne by the contractor (the tenant). Detailed Host/Tenant Agreements and Site Activation Plans between both the principal and secondary test sites and the contractor shall be prepared in accordance with NAVAIRINST 4000.15A and will be utilized to define the specific resources available to the contractor at each test site.

(b) **(REDACTED)** The contractor shall have use of work spaces at both the Naval Air Test Center and Naval Weapons Center for which the minimum square footage is specified below. Program plans for ATA FSD effort include construction of new hangar spaces at both test sites. In the event that construction of the hangar facilities is not complete by the

scheduled arrival dates, adequate interim facilities will be provided to the contractor until the new construction is completed at which time the contractor will be moved into the new spaces. The contractor shall plan for and execute an orderly transition into the new spaces at such time as they become available such that no impact on the flight test program shall occur. Host facilities and services will be made available to support the move. The contractor shall supply and install special laboratory and test equipment to be listed in his Site Activation Plan for each of the test sites. Physical security of all contractor assigned spaces shall be the responsibility of the contractor.

	NATC (sq ft)	NWC (sq ft
Office and Computer Space	9,000	2,000
Warehouse and Storage Space	5,000	1,100
Laboratory Space	12,000	3,800
Aircraft Shop Areas	7,500	3,500
Project Hangar Space	26,000	10,400
	59,500	20,800

In addition, the Government will furnish at the above installation:

(a) Necessary fuel trucks
(b) Electricity
(c) Water

(d) Gas
(e) Compressed Air
(f) Sewer
(g) Fire Protection
(h) Security
(i) Telephone service, excluding toll calls
(j) Maintenance space and shop usage
(k) Hangar space
(l) All additional services, facilities and equipment usage documented in Host/Tenant Agreements and subsequent FRD's.

(c) (U) Additional Government installations to be provided hereunder on a rent-free non-interference basis, along with requirement dates for all installations are listed below:

NOMENCLATURE	NEED DATES FROM/TO	UTILIZATION
AMES RESEARCH CENTER (ARC)	06-01-88/06-30-88 08-01-88/09-15-88 01-01-89/02-15-89 05-01-89/06-15-89 08-01-89/09-15-89 01-01-90/02-15-90 04-01-91/04-30-91	WIND TUNNEL
NASA LANGLEY RESEARCH CENTER (LRC) NTF	01-01-90/02-15-90	WIND TUNNEL

(LRC) SPIN	10-01-88/12-15-88	
	00-01-90/00-02-90	
	00-02-90/00-03-90	
	09-01-90/10-15-90	
(LRC) 30X60	08-01-88/09-15-88	
	INTERMITTENT	
	TO 10-15-88	
	08-01-89/08-31-89	
(LRC) TDT	09-01-88/10-15-88	
	09-01-89/09-30-89	
	05-01-90/05-31-90	
ARNOLD ENGINEERING DEVELOPMENT CENTER	02-01-88/03-15-88	PWT 16T WIND TUNNEL
	07-01-88/08-15-88	
	09-01-88/11-30-88	
	03-01-89/03-31-89	
	07-01-89/07-31-89	
	09-01-89/	
	INTERMITTENT	
	TO 01-31-90	
	10-01-90/10-31-90	
LEWIS RESEARCH CENTER (LERC) (6x9 ft. icing tunnel) NAEC LAKEHURST, N.J.	09-01-88/10-31-88	WIND TUNNEL
	10-01-90/03-31-91	FLIGHT TEST
	02-01-91/10-31-91	BARRICADE ENGAGE-MENT

	01-01-93/06-01-93	
NATC (PAX)	06-01-90/04-30-93	STRUCTURAL DYNAMICS
	01-01-90/04-30-93	FLIGHT TEST
NAVY WEAPON CENTER (CHINA LAKE)	06-01-88/07-31-88	SURV/ VULN-BALLISTICS
	06-01-89/07-31-89	
	03-01-91/03-31-91	
	01-01-92/03-31-92	
	11-01-89/01-31-90	SLED TEST
	06-01-90/10-31-93	FLIGHT TEST
NADC	07-01-89/07-31-89	EJECTION TOWER TESTS
TRENTON, N.J. NAPC	07-01-89/06-30-90	PROPULSION TESTS

NOMENCLATURE	NEED DATES	UTILIZATION
U.S.ARMY PROVIDING GROUNDS (DUBWAY, UT.)	09-01-88/10-31-88	SURV/VULN CBR
AF - EWES	06-01-88/05-31-89	SIMULATION
RATSCAT - RAMS	12-15-87/07-31-88	SIGNATURE TEST
	05-01-88/08-31-88	
APPROPRIATE SIGNATURE TEST FACILITY	AS REQUIRED	
EDWARDS AFB	10-01-92/12-31-92	FLIGHT TEST CROSS WINDS
EGLIN AFB	10-01-92/12-31-92	CLIMATIC TEST

(3) (U) All government-furnished Search and Rescue Aircraft, test equipment, ground stations, and Special Flight Test Instrumentation (SFTI), as identified in Addendum 116 to MIL-D-87088.

(4) (U) Aircrew and maintenance trainer facilities including air conditioning, heating, lighting, adequate electric power and grounding, and

raised flooring (aircrew only), on the dates provided below.

Trainer Suite	Need Date
Site #1	July 1992
Site #2	March 1995
Site #3	July 1995

(f) (U) Bailed Property to be Used Under this Contract. (This paragraph will not obviate the need to set forth in this contract the terms of the project agreement as required by the pertinent bailment agreement.)

(1) (U) The bailed property identified in (f) (2) is hereby authorized for use on a rent-free basis in the performance of this contract. Although not "Government-furnished property" under this contract, the provisions of paragraph (a) of the Government Property clause of this contract shall apply to this bailed property.

(2) (U)

Description	Serial Number	Bailment Agreement Under Which Accountable
NONE		

(3) (U) The bailed property identified in (f) (2) is furnished "as is" and the Government makes no representations or warranties with respect to such property, including the suitability of such property for the intended use.

(g) (U) Notwithstanding any provision to the contrary in any contract with the United States Government and in order to ensure compliance with 22 U.S.C. 2761(e), rent-free use of any property identified above (other than that property identified in paragraph (d)) in the performance of work under this contract to satisfy an obligation that implements a sale of goods or services, or both, to a foreign government or international organization (if called for under this contract) is expressly prohibited. Further, this contract shall in no event be construed to authorize rent-free use of any property identified above in the performance of direct commercial sales to a foreign government or international organization.

(h) (U) Installation Cost. The price of this contract constitutes full compensation to the Contractor for all costs to be incurred under this contract for the adaptation and installation of the property identified in this clause.

(i) (U) Installation. Government production and research property, other than foundations and similar improvements necessary for the installation of special tooling, special test equipment, and plant equipment, as defined in FAR 45.101, shall not be installed or constructed on land not owned by the government in such fashion as to be non-severable unless authority is granted by the Contracting Officer cognizant of the contract under which the property is provided in accordance with FAR 45.309.

(j) (U) Limitation. This clause does not authorize the Contractor to acquire any property for the Government.

(k) (U) The Contractor represents that the price and delivery schedule of this contract have been established in reliance on the Government granting the authorization in (b), (c), (d), (e) and (f) and that no charge has been included in this contract for use of the property as authorized above.

(l) (U) Whenever the Contracting Officer authorizes or makes available the use, on a rent-free basis, of additional Government production and research property or other Government property in the performance of this contract or subcontracts of any tier under this contract, the contract will be equitably adjusted in accordance with the procedures provided for in the Changes clause.

(m) (U) If the Government production and research property or other Government property authorized or made available above is decreased by the Government, the Contractor will be entitled to an equitable adjustment to the terms of this contract in accordance with the procedures provided for in the Changes clause hereof as a result of such decrease; provided, however, that if any such decrease is due to the failure of the Contractor or his subcontractors of any tier under this contract to fulfill their respective obligations either with respect to the Government property or with respect to the work such property is to be used to perform, the Contracting Officer will

take such circumstances into account in establishing the equitable adjustment.

(END OF CLAUSE)

H-29 (U) GOVERNEMENT-FURNISHED PETROLEUM, OIL, AND LUBRICANTS

(a) **(REDACTED)** The petroleum, oil and lubricant items necessary for use in the performance of this contract set forth below and in SD-574-1, Appendix E, shall be furnished by the Government to the Contractor subject to the provisions of this clause and the "Government Property for the Performance of this Contract" clause for use at Contractor designated plants at Tulsa, Oklahoma; St. Louis, Missouri; Forth Worth, Texas; Lynn, Massachusetts; Evandale, Ohio; or Trenton, New Jersey, as applicable, and for use at the Government installations listed in Clause H-28.

Aviation Turbine Fuel, commercial Grade JP-4 Type MIL-T-5624L, NSN 9130-00-256-8613

Aviation Turbine Fuel, Commercial Grade JP-5 Type MIL-T-5624L, NSN 9130-00-273-2379

Aviation Turbine Lubricating Oil Type MIL-L-23699 NSN 9150-00-681-5999

Aviation Turbine Lubricating Oil, Grade 1010, Type MIL-L-6081, NSN 9150-00-231-6676

(b) (U) In the event a situation or condition arises whereby the Government is unable to furnish the petroleum, oil, or lubricant items in a timely manner so that a delay in the performance of the contract is threatened, it is agreed that the Contractor shall, with the approval of the Administrative Contracting Officer, procure the necessary petroleum, oil, and lubricant items to prevent delay in performance of the contract. The Contractor may either receive reimbursement in kind, or be entitled to an equitable adjustment to all relevant terms of the contract in accordance with the procedures provided for in the "changes" clause to take into account the contractor's having provided such fuel, petroleum or lubricant.

(REDACTED) Estimated quantities of Aviation Turbine Fuel, MIL-T-5624L are as follows:

	Quantity in Barrel's
FSD	425,000*
Lot 1	2,640
Lot 2	3,520
Lot 3	8,800
Lot 4	15,840

(c) (U) The Contractor shall comply with MIL-STD-1518A, dated 20 February 1974.

(END OF CLAUSE)

H-30 (U) SPECIAL INSTRUCTIONS PERTAINING TO CERTAIN GOVERNMENT FURNISHED PROPERTY

(U) The Government will furnish to the Contractor for use in the performance of this contract, subject to and in accordance with the provisions of the clause entitled "Government Property for the Performance of this Contract," the following:

AIRCRAFT LOG BOOK BINDERS AND SEPARATION PAGES

ENGINE LOG BOOK BINDERS AND SEPARATION PAGES

(U) The Administrative Contracting Officer (ACO) shall insure that aircraft and engine log book binders and separation pages are available for at least ninety (90) days prior to the delivery of the aircraft and/or engine for which they are associated.

(REDACTED) In the event an aircraft or engine log book binder and separation pages is not available at that time, the ACO shall contact Naval Weapons Engineering Support Activity, Washington D.C. 20734, Attn ESA-203 to furnish as required.

(END OF CLAUSE)

H-31 **(REDACTED)** PROCEDURE FOR OBTAINING CONTROLLED MATERIALS (MAY 1986) (NAVAIR 52.212-9500)

(U) Increasing scarcity of production materials demands that the following procedures be adhered to in complying with the requirements of the clause of this contract entitled "Defense Priority and Allocation Requirements". Nonconformance with these procedures may cause delays in obtaining needed materials --

(a) (U) The priority rating must appear on all subcontracts and purchase orders.
(b) (U) Adequate delivery lead time must be allowed in placing subcontracts and purchase orders.
(c) (U) The Contractor shall use his best efforts to obtain a satisfactory delivery schedule from his subcontractors prior to referral to the Government for assistance. Such referral, if required, shall be made to the Administrative Contracting Officer of the cognizant contract administration office.

PART II – CONTRACT CLAUSES

PROGRESS PAYMENTS (APR 1984) (DEVIATION) (FAR 52.232-16)

Progress payments shall be made to the Contractor when requested as work progresses, but not more frequently than monthly in amounts approved by the Contracting Officer, under the following conditions:

(a) Computation of amounts

(1) Unless the Contractor requests a smaller amount, each progress payment shall be computed as

(i) 75 percent of the Contractor's cumulative total costs under this contract, as shown by records maintained by the Contractor for the purpose of obtaining payment under Government contracts, plus

(ii) progress payments to subcontractors (see paragraph (j) below), all less the sum of all previous progress payments made by the Government under this contract. Cost of money that would be allowable under 31.205-10 of the Federal Acquisition Regulation shall be deemed an incurred cost for progress payment purposes.

(2) The following conditions apply to the timing of including costs in progress payment requests:

(i) The costs of supplies and services purchased by the Contractor directly for this contract may be included only after payment by cash, check, or other form of actual payment.

(ii) Costs for the following may be included when incurred, even if before payment, when the Contractor is not delinquent in payment of the costs of contract performance in the ordinary course of business:

(A) Materials issued from the Contractor's stores inventory and placed in the production process for use on this contract.

(B) Direct labor, direct travel, and other direct in-house costs.

(C) Properly allocable and allowable indirect costs.

(iii) Accrued costs of Contractor contributions under employee pension, profit sharing, and stock ownership plans shall be excluded until actually paid unless –

(A) The Contractor's practice is to contribute to the plans quarterly or more frequently; and

(B) The contribution does not remain unpaid 30 days after the end of the applicable quarter or shorter payment period (any contributions remaining unpaid shall be excluded from the Contractor's total costs for progress payments until paid).

(iv) If the contract is subject to the special transition method authorized in Cost Accounting Standard (CAS) 410, Allocation of Business Unit General and Administrative Expense to Final Cost Objective, General and Administrative expenses (G&A) shall not be included in progress payment requests until the suspense account prescribed in CAS 410 is less than –

(A) Five million dollars; or

(B) The value of the work-in-process inventories under contracts entered into after the suspense account was established (only a pro rata share of the G&A allocable to the excess of the inventory over the suspense account value is includable in

progress payment requests under this contract).

(3) The Contractor shall not include the following in total costs for progress payment purposes in subparagraph (a)(1)(i) above:

(i) Costs that are not reasonable, allocable to this contract, and consistent with sound and generally accepted accounting principles and practices.

(ii) Costs incurred by subcontractors or suppliers.

(iii) Costs ordinarily capitalized and subject to depreciation or amortization except for the properly depreciated or amortized portion of such costs.

(iv) Payments made or amounts payable to subcontractors or suppliers, except for –

(A) Completed work, including partial deliveries, to which the Contractor has acquired title; and

(B) Work under cost-reimbursement or time-and-material subcontracts to which the Contractor has acquired title.

(4) The amount of unliquidated progress payments may exceed neither (i) the progress payments made against incomplete work (including allowable unliquidated progress payments to subcontractors) nor (ii) the value, for progress payment purposes, of the incomplete work. Incomplete work shall be considered to be the supplies and services required by this contract, for which delivery and invoicing by the Contractor and acceptance by the Government are incomplete.

(5) The total amount of progress payments shall not exceed 75 percent of the total contract price.

(6) If a progress payment or the unliquidated progress payments exceed the amounts permitted by subparagraphs (a)(4) or (a)(5) above, the Contractor shall repay the amount of such excess to the Government on demand.

(b) Liquidation. Except as provided in the Termination for Convenience of the Government clause, all progress payments shall be liquidated by deducting from any payment under this contract, other than advance or progress payments, the unliquidated progress payments, or 75 percent of the amount invoiced, whichever is less. The Contractor shall repay to the Government any

amounts required by a retroactive price reduction, after computing liquidations and payments on past invoices at the reduced prices and adjusting the unliquidated progress payments accordingly. The Government reserves the right to unilaterally change from the ordinary liquidation rate to an alternate rate when deemed appropriate for proper contract financing.

(c) Reduction or suspension. The Contracting Officer may reduce or suspend progress payments, increase the rate of liquidation, or take a combination of these actions, after finding on substantial evidence any of the following conditions:

(1) The Contractor failed to comply with any material requirement of this contract (which includes paragraphs (f) and (g) below).

(2) Performance of this contract is endangered by the Contractor's (i) failure to make progress or (ii) unsatisfactory financial condition.

(3) Inventory allocated to this contract substantially exceeds reasonable requirements.

(4) The Contractor is delinquent in payment of the costs of performing this contract in the ordinary course of business.

(5) The unliquidated progress payments exceed the fair value of the work accomplished on the undelivered portion of this contract.

(6) The Contractor is realizing less profit than that reflected in the establishment of any alternate liquidation rate in paragraph (b) above, and that rate is less than the progress payment rate stated in subparagraph (a)(1) above.

(d) Title. (1) Title to the property described in this paragraph (d) shall vest in the Government. Vestiture shall be immediately upon the date of this contract, for property acquired or produced before that date. Otherwise, vestiture shall occur when the property is or should have been allocable or properly chargeable to this contract.

(2) "Property," as used in this clause, includes all of the below-described items acquired or produced by the Contractor that are or should be allocable or properly chargeable to this contract under sound and generally accepted accounting principles and practices.

(i) Parts, materials, inventories, and work in process;

(ii) Special tooling and special test equipment to which the Government is

to acquire title under any other clause of this contract;

(iii) Nondurable (i.e., noncapital) tools, jigs, dies, fixtures, molds, patterns, taps, gauges, test equipment, and other similar manufacturing aids, title to which would not be obtained as special tooling under subparagraph (ii) above; and

(iv) Drawings and technical data, to the extent the Contractor or subcontractors are required to deliver them to the Government by other clauses of this contract.

(3) Although title to property is in the Government under this clause, other applicable clauses of this contract, e.g., the termination or special tooling clauses, shall determine the handling and disposition of the property.

(4) The Contractor may sell any scrap resulting from production under this contract without requesting the Contracting Officer's approval, but the proceeds shall be credited against the costs of performance.

(5) To acquire for its own use or dispose of property to which title is vested in the Government under this clause, the

Contractor must obtain the Contracting Officer's advance approval of the action and the terms. The Contractor shall (i) exclude the allocable costs of the property from the costs of contract performance, and (ii) repay to the Government any amount of unliquidated progress payments allocable to the property. Repayment may be by cash or credit memorandum.

(6) When the Contractor completes all of the obligations under this contract, including liquidation of all progress payments, title shall vest in the Contractor for all property (or the proceeds thereof) not--

(i) Delivered to, and accepted by, the Government under this contract; or

(ii) Incorporated in supplies delivered to, and accepted by, the Government under this contract and to which title is vested in the Government under this clause.

(7) The terms of this contract concerning liability for Government-furnished property shall not apply to property to which the Government acquired title solely under this clause.

(e) Risk of loss. Before delivery to and acceptance by the Government, the Contractor

shall bear the risk of loss for property, the title to which vests in the Government under this clause, except to the extent the Government expressly assumes the risk. The Contractor shall repay the Government in amount equal to the unliquidated progress payments that are based on costs allocable to property that is damaged, lost, stolen, or destroyed.

(f) Control of costs and property. The Contract shall maintain an accounting system and controls adequate for the proper administration of this clause.

(g) Reports and access to records. The Contractor shall promptly furnish reports, certificates, financial statements, and other pertinent information reasonably requested by the Contracting Officer for the administration of this clause. Also, the Contractor shall give the Government reasonable opportunity to examine and verify the Contractor's books, records, and accounts.

(h) Special terms regarding default. If this contract is terminated under the Default clause, (i) the Contractor shall, on demand, repay to the Government the amount of unliquidated progress payments and (ii) title shall vest in the Contractor, on full liquidation of progress payments, for all property for which the Government elects not to require delivery under the Default clause. The

Government shall be liable for no payment except as provided by the Default clause.

(i) Reservations of rights. (1) No payment or vesting of title under this clause shall (i) excuse the Contractor from performance of obligations under this contract or (ii) constitute a waiver of any of the rights or remedies of the parties under the contract.

(FAR 52.232-16) (DEVIATION)

(2) The Government's rights and remedies under this clause (i) shall not be exclusive but rather shall be in addition to any other rights and remedies provided by law or this contract and (ii) shall not be affected by delayed, partial, or omitted exercise of any right, remedy, power, or privilege, nor shall such exercise or any single exercise preclude or impair any further exercise under this clause or the exercise, of any other right, power, or privilege of the Government.

(j) Progress payments to subcontractors. The amounts mentioned in (a)(1)(ii) above shall be all progress payments to subcontractors or divisions, if the following conditions are met:

(1) The amounts included are limited to (i) the unliquidated remainder of progress payments made plus (ii) for small business concerns any unpaid subcontractor

requests for progress payments that the Contractor has approved for current payment in the ordinary course of business.

(2) The subcontract or interdivisional order is expected to involve a minimum of approximately 6 months between the beginning of work and the first delivery, or, if the subcontractor is a small business concern, 4 months.

(3) The terms of the subcontract or interdivisional order concerning progress payments--

(i) Are substantially similar to the terms of the clause at 52.232-16 Progress Payments, of the Federal Acquisition Regulation (or that clause with its Alternate I for any subcontractor that is a small business concern);

(ii) Are at least as favorable to the Government as the terms of this clause;

(iii) Are not more favorable to the subcontractor or division than the terms of this clause are to the Contractor;

(iv) Are in conformance with the requirements of paragraph 32.504(e) of the Federal Acquisition Regulation; and

(v) Subordinate all subcontractor rights concerning property to which the Government has title under the subcontract to the Government's right to require delivery of the property to the Government if (A) the Contractor defaults or (B) the subcontractor becomes bankrupt or insolvent.

(4) The progress payment rate in the subcontract is the customary rate used by the Contracting Agency, depending on whether the subcontractor is or is not a small business concern.

(5) The parties agree concerning any proceeds received by the Government for property to which title has vested in the Government under the subcontract terms, that the proceeds shall be applied to reducing any unliquidated progress payments by the Government to the Contractor under this contract.

(6) If no unliquidated progress payments to the Contractor remain, but there are unliquidated progress payments that the Contractor has made to any subcontractor, the Contractor shall be subrogated to all the rights the Government obtained through the terms required by this clause to be in any subcontract, as if all such rights had been assigned and transferred to the Contractor.

(7) The Contractor shall pay the subcontractor's progress payment request under subdivision (j)(1)(ii) above, within a reasonable time after receiving the Government progress payment covering those amounts.

(8) To facilitate small business participation in subcontracting under this contract, the Contractor agrees to provide progress payments to small business concerns, in conformity with the standards for customary progress payments stated in Subpart 32.5 of the Federal Acquisition Regulation. The Contractor further agrees that the need for such progress payments shall not be considered as a handicap or adverse factor in the award of subcontracts.

INVOICES (OCT 1982) (DOD FAR SUP 52.232-7000)

(a) An invoice is a written request for payment under the contract for supplies delivered or for services rendered. In order to be proper, an invoice must include as applicable the following:

(1) invoice date;

(2) name of contractor;

(3) contract number (including order number, if any), contract line item number, contract description of supplies or services, quantity, contract unit of measure and unit price, and extended total;

(4) shipment number and date of shipment (bill of lading number and weight of shipment will be shown for shipments on Government bills of lading);

(5) name and address to which payment is to be sent (which must be the same as that in the contract or on a proper notice of assignment);

(6) name (where practicable), title, phone number and mailing address of person to be notified in event of a defective invoice; and

(7) any other information or documentation required by other provisions of the contract (such as evidence of shipment).

Invoices shall be prepared and submitted in quadruplicate (one copy shall be marked "original") unless otherwise specified.

(b) For purposes of determining if interest begins to accrue under the Prompt Payment Act (Public Law 97-177):

(1) a proper invoice will be deemed to have been received when it is received by the office designated in the contract for receipt of invoices and acceptance of the supplies delivered or services rendered has occurred;

(2) payment shall be considered made on the date on which a check for such payment is dated;

(3) payment terms (e.g., "net 20") offered by the Contractor will not be deemed a "required payment date;" and

(4) the following periods of time will not be included

(i) after receipt of an improper invoice and prior to notice of any defect or impropriety, but not to exceed 15 days (or any lesser period established by this contract); and

(ii) between the date of a notice of any defect or impropriety and the date a proper invoice is received. When the notice is in writing, it shall be considered made on the date shown on the notice.

FLEXIBLE PROGRESS PAYMENTS (MAY 1985) (DOD FAR SUP 52.232 7004)

This contract is subject to flexible progress payment procedures. The progress payment rate of this contract is %, and this percentage applies in lieu of the uniform standard progress payment rate and liquidation rate of the "Progress Payments" clause. The progress payment rate of this contract was determined by the DOD Cash Flow Computer Model, dated , using twenty-five percent (25%) as the targeted rate for the contractor's investment (as a weighted average of costs) in its work in process inventory over the life of the contract.

If actual and projected cash flow data generated during performance of this contract reveal that the progress payment rate will result in an investment in work in process inventory by the contractor in excess of twenty seven percent (27%), or less than twenty three percent (23%), the progress payment rate shall be redetermined by using the DOD Cash Flow Computer Model. Unless it contained an error, the version of the DOD Cash Flow Computer Model that was used initially in this contract will be used for any redetermination permitted by the clause. In no event will the progress payment rate be less than the uniform standard progress payment rate that would have applied to this contract absent flexible progress payment procedures, and in no event will the progress payment rate be greater than one hundred percent (100%).

As of the date of execution of this contract, the initial progress payment rate has not been determined. However, the price of this contract is

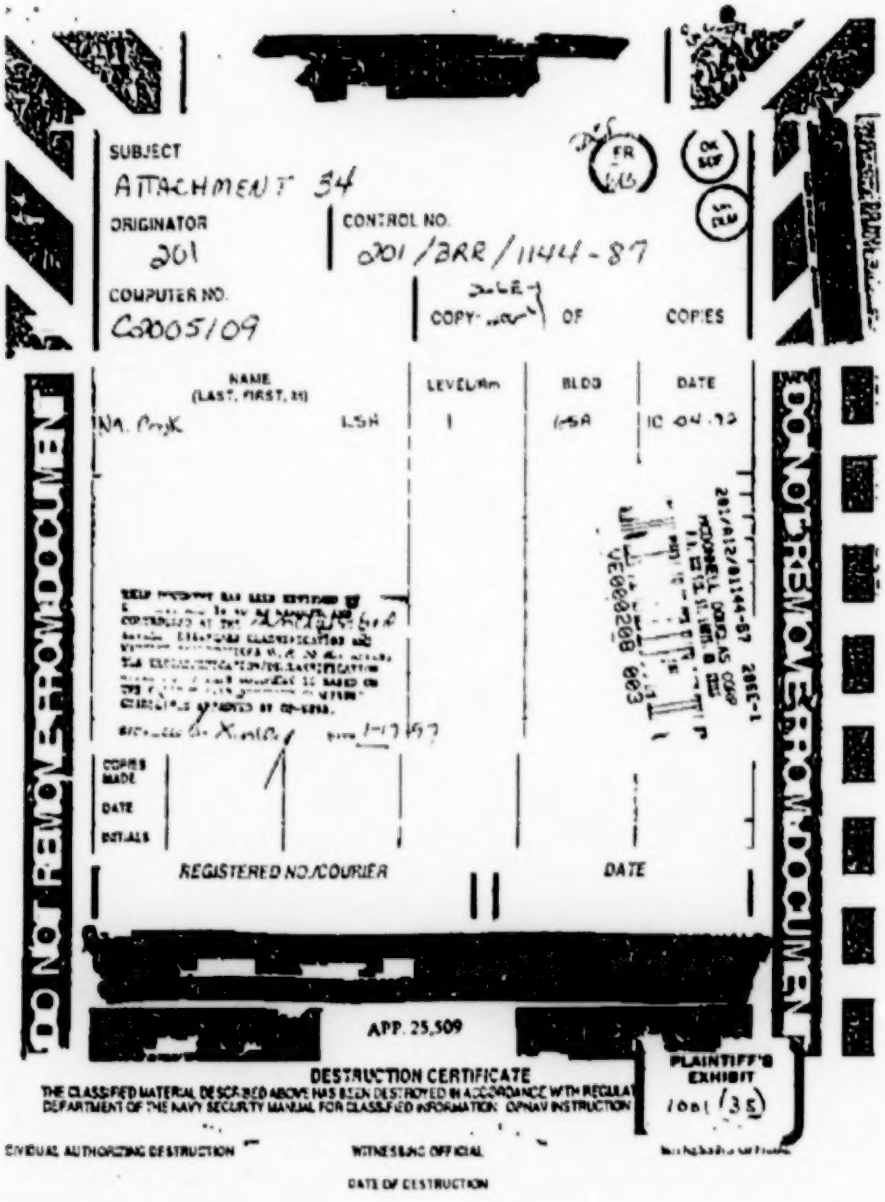
based on flexible progress payments. Promptly upon contract award, the Contractor shall provide data supporting flexible progress payments percentage calculation. The flexible progress payments percentage shall be calculated, agreed upon between the parties and inserted by bilateral modification within 60 days after Contractor provides the data as above. Failure to agree shall be considered a dispute within the meaning of the "Disputes" clause hereof. Pending the above, the Contractor shall invoice based on standard progress payments of General Provision 52.232-16.

ORDER OF PRECEDENCE (CONTRACT) (APR 1985) (NAVAIR 52.290-9500)

Inn the event of an inconsistency in this contract unless otherwise provided herein, the inconsistency shall be resolved by giving precedence in the following order: (a) the Schedule (excluding the Specifications); (b) contract clauses; (c) the other provisions of the contract whether incorporated by reference or otherwise; and (d) the Specifications.

SUBCONTRACTING (APR 1985) (NAVAIR 52.244-9501)

The Contractor shall not acquire any of the completed articles described herein, except spare parts, from any other party, either by subcontract or otherwise without the prior written consent of the Contracting Officer.



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NAVAL AIR SYSTEMS COMMAND

DEPARTMENT OF THE NAVY

CONTRACT SECURITY CLASSIFICATION SPECIFICATION

DD FORM 254

FOR THE

ATA

AIRCRAFT WEAPON SYSTEM

01 DECEMBER 1987

ATTACHMENT 34 **[REDACTED]**

[REDACTED]	201/BRR/1144-87
	13 TOTAL PAGES
[REDACTED]	COPY OF COPIES

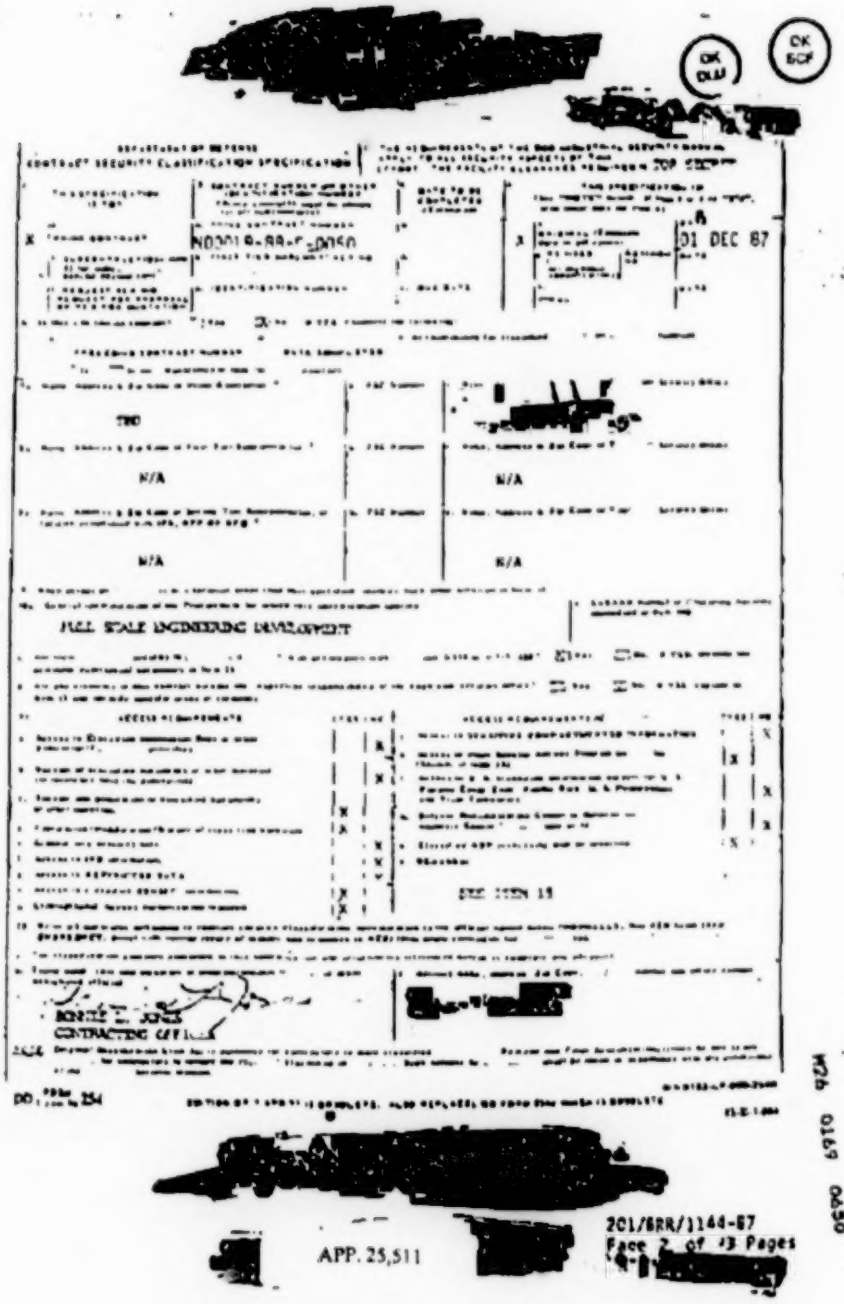
[redacted]

OK DLM

OK SCF

[redacted]

DEPARTMENT OF DEFENSE
CONTRACT SECURITY CLASSIFICATION SPECIFICATION



X	N00019-88-C-0050	X	01 DEC 87

TBD		[redacted]
N/A		N/A
N/A		N/A

FULL SCALE ENGINEERING DEVELOPMENT

ACCESS REQUIREMENTS			ACCESS REQUIREMENTS		
		X			X
		X		X	
	X				X
	X				X
		X		X	
		X			
	X				
	X				

SEE ITEM 15

BONNIE L. JONES
CONTRACTING OFFICER

[redacted]

DD FORM 254

[redacted]

APP. 25,511

201/BRR/1144-87
Page 2 of 13 Pages

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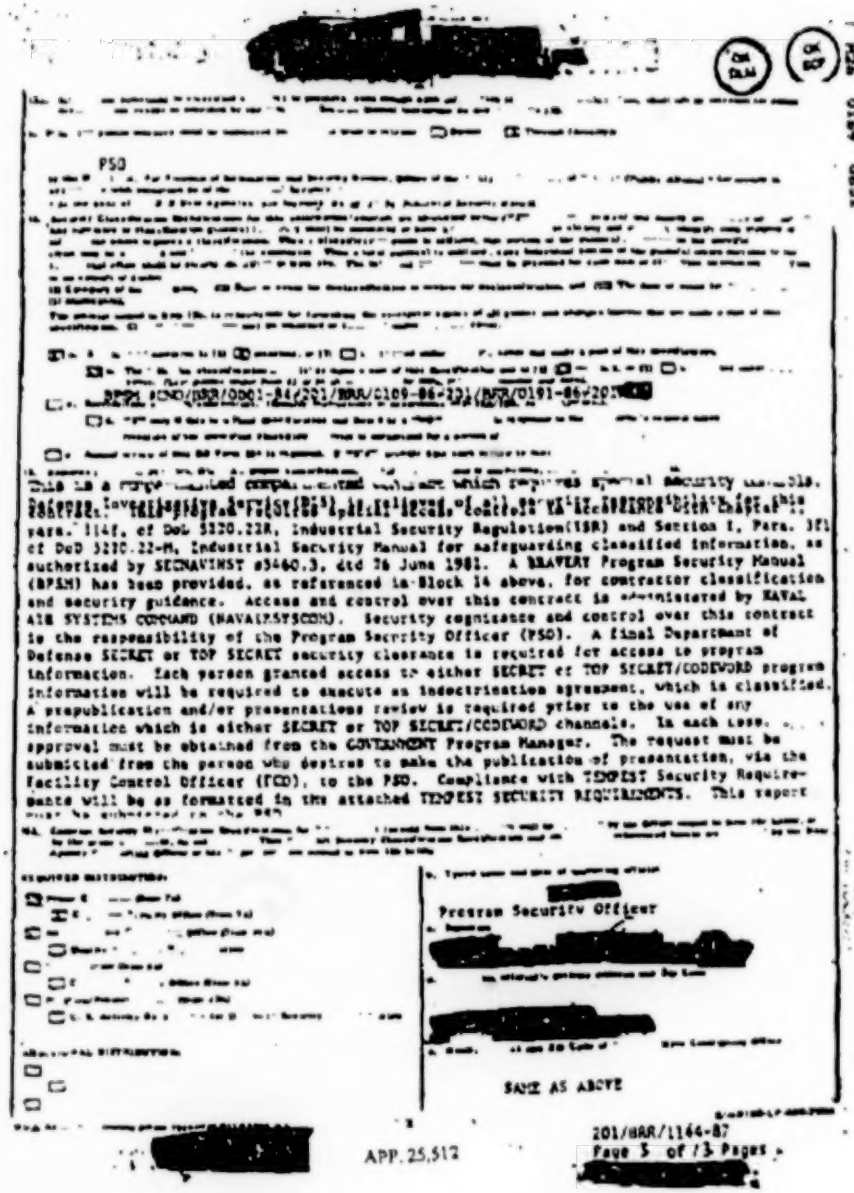

PSO

Program Security Officer

SAME AS ABOVE

[REDACTED]

[REDACTED] A special security restrictions clause is contained in Section H of the contract and applies to the handling of classified information under this contract, compartmented or otherwise.

[REDACTED] Security guidelines are contained in the Bravery Program Security Manual that has been previously provided.

[REDACTED] Material not properly falling under this special access compartmented program shall be handled in accordance with the instructions provided by the Bravery Program Security Officer.

(U) The guidance contained herein and in the Program Security manual and the Program Security Guidelines will be utilized in conjunction with any further guidance provided by the Bravery Program Manager and the Bravery Program Security Officer.

[REDACTED] No external distribution of any documents will be made without the explicit written approval of the Program Manager. All documents, working papers, and copies of deliverables will be returned to the Program Manager upon completion of this contract. The contractor is not authorized to retain any Bravery Program related documentation upon completion of this contract. All Government furnished documents will be returned to the appropriate Government source upon completion of this contract.

(U) All subcontracting by the prime contractor involving classified information and/or hardware which requires attendent DD-254's, will be reviewed by the Program Security Officer, prior to issuance.

(U) Program documents and materials will only be stored in facilities specifically approved by the Program Security Officer.

[REDACTED] Tests will be conducted in such a manner as to insure maximum security for the Bravery Project and test sites will be approved by the Program Security Officer.

(U) Items 11K and 14: All material generated under this contract shall perpetuate the classification downgrading and declassification of the source material. Newly generated material, no source documents, shall contain the following downgrading statement:

[REDACTED]

[REDACTED] Final classification review and determination will be the responsibility of the Bravery Program Manager.

[REDACTED] All contractors participating in the Bravery Program must possess, or be eligible to possess, a Department of Defense Facility Security Clearance in accordance with Section III, paragraphs 21 and 22, of the Industrial Security Manual, DoD 5220.22-M. The Bravery Program Security Officer is the approving authority for Bravery access of a

contractor's facility, and conducts security review for Bravery personnel accesses.

[REDACTED]	SECTION 15-REMARKS CONTINUED	
[REDACTED]	201/BRR/1144-87	Page 1 of 2
[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	APP.25,513	[REDACTED]

[REDACTED] TEMPEST security requirements, (see enclosure 1), are imposed if any electrical processing of classified information is required in contract performance. Support in complying with this requirement is available upon request from the [REDACTED] Program Security Officer.

[REDACTED]

SECTION 15-REMARKS CONTINUED
Page 2 of 2

[REDACTED]

[REDACTED]

ATTACHMENT 36

GOVERNMENT FURNISHED PROPERTY

FSD AND LOTS 1-4

SECTION 1: GOVERNMENT FURNISHED INFORMATION

SECTION 2: LAND BASE EQUIPMENT (SECURE VOICE COMMUNICATION)

SECTION 3: ORDNANCE

SECTION 4: SUPPORT EQUIPMENT

- LOTS 2 THRU 4

SECTION 5: SUPPORT EQUIPMENT

- FSD & LOT 1

Section 1: GOVERNMENT FURNISHED INFORMATION (U)

NOMENCLATURE	NEED DATE
NWC-1432 A-6E/AGM-65E Laser Maverick Weapon System Integration Requirements and Development Specification dated 23 Oct 1983 (or latest revision)	1-15-88
NWC-1433 A-6E/AGM-65F Design Infrared Maverick Weapon System Integration Requirements and Development Specification dated 26 Oct 1983	1-15-88
NWC-1434 A-6E/Harpoon Block 1C Weapon System Integration Requirements and Development Specification dated 24 Oct 1983 (or latest revision)	1-15-88
NWC-1497 A-6E/Post Launch Controlled Weapon System Integration Requirements and Development Specification dated 9 Jan 1984 (or latest revision)	1-15-88
SWLA DWG 185474 Basic	12-15-87

NOMENCLATURE	NEED DATE
Interface Requirement System/Rev E (or latest revision)	
A-6E Navy Training Plan (NTP) 1 + Revisions	Jan 88

NOMENCLATURE	NEED DATE
A-6E Squadron Manning Document (10 Aircraft - if available) 1 - Revision	Jan 88
A-6F Navy Training Plan (NTP) 1 = Revisions	Jan 88
On-the-job Training Handbook for Preliminary Squadron Manpower Document Development (OJT PSQMD) 1 + Revisions	Jan 88
Tech Pubs required for Support Equipment being furnished by the Government	Jan 88 (Program Go-Ahead) thru end of OPEVAL
Tech Pubs required for Common Support Equipment being procured as CFE by the Contractor for FSD and Lot 1	Jan 88 (Program Go-Ahead) thru end of OPEVAL
Tech Pubs required for	Jan 88 (Program

NOMENCLATURE	NEED DATE
Airborne GFE Equipment being furnished by the Government for FSD and Lot 1	Go-Ahead) thru end of OPEVAL
Tech Pubs required for Airborne GFE Equipment being procured as CFE by the Contractor for FSD and Lot 1	Jan 88 (Program Go-Ahead) thru end of OPEVAL

NOMENCLATURE	NEED DATE
Interface and Integration data for the following weapons: (a) Advanced Air-to-Air Missile (AAAM) (b) Advanced Interdiction Weapon System (AIWS) (c) **[REDACTED]** (d) Standoff Land Attack Missile (SLAM) (e) Store Dispenser (SUU-25) (f) Advanced Anti-Radiation Missile (AdARM) Including, but not limited to: (a) Interface Control Documents Interface Requirements Specifications	2nd Qtr Cy 88

NOMENCLATURE	NEED DATE
(c) Prime Item Development Specifications	
(d) System Segment Specifications	

Section 5: SUPPORT EQUIPMENT - FSD & LOT 1

COMMON SUPPORT EQUIPMENT AT PATUXENT RIVER

The following support equipment will be provided by the Government on an as needed basis from the respective base pool assets.

PART NO.	NOMENCLATURE	NSN
517AS300	Hoist Unit, Bomb (HLU196B/E)	1730-00-123-6749
630AS100-11	Service Unit, Hyd Hand Pump	1730-01-088-4611
A/C Towing	1740-00-414-7150	Tractor, Wheeled,
TA75B		
		Set, Borescope Lt
Sce (50,	6650-01-138-1711	
21C8559P01	60, 400 HZ)	
65A102J1	Cart, Corrosion Control	4920-00-930-1801

COMMON SUPPORT EQUIPMENT AT CHINA LAKE

PART NO.	NOMENCLATURE	NSN
1317AS100-1	N2 Serving unit	3655-01-112-4943

630AS100-11	Service Unit, Hyd Hand Pump	1730-01-088-4611
Hydraulic	4320-01-098-6713	Pumping Unit,
D12025-001		
TA75B	Tractor, Wheeled, A/C Towing	1740-00-414-7150
Calibrator	6605-00-032-6306	Compass
2591553-901		
3100404-001-103	[REDACTED]	6625-01-204-4292

SUPPORT EQUIPMENT PECULIAR TO MCAIR/GDFW AT CHINA LAKE

PART NO.	NOMENCLATURE	NSN
1058AS100	Test Set, AIM-9 Missile, ANASM464	4935-01-049-3596
1128AS100	Jack, Hand Hyd, 20TON	1730-01-109-1146
1317AS100-1	N2 Service Unit	3655-01-112-4943
1502-04	Reflectometer, Time	6625-01-037-4412
1567575	Adapter, Soft Belt (Acro 64A)	1730-00-948-3532

	A/C Mobile Electric (NR-5C)	4120-01-208-8705
1603AS100-1		
	Test Set Firing Circuit	4920-00-152-1997
178AS100		
2001MCV	Fluid Makeup Unit, Liq Cool	4920-01-092-7266
215-00303-50	Dolly-Multi Purpose	1730-00-133-9417
223	Pneumatic Injection Sealant Gun	5130-00-941-9976
	Adapter, Sealant Gun	5120-00-941-9976
226358		

	Multimeter	6625-01-021-0236
260-6XLP		
4918A	Leak Detector, Ultrasonic	6625-00-960-5062
53992	Key, Pin - Ejection seat	1730-01-163-5300
	Air Cylinder, Port	1730-00-625-6872
60A80D1		
61A101D	Tiedown, Aircraft	1730-00-572-7370
	Aero-58A Adapter, Front	1740-00-754-4804
64A114D16-1		
64A114D17-1	Aero-58A Adapter, Rear	1740-00-675-6031
64A114D322-1	Single Stores Adapter (ADU-498/E)	1730-01-174-1885
	Skid Weapon (Aero 21C)	1740-00-148-6492
64A114H1		
64A127J1-1	Cradle, Transport, Ej Seat	1730-00-944-5498
66A79J1	Small Bomb and Missile ADP (AERO67A)	1730-00-832-8562
68A4J1000-1	TS-Hyd Port, Diesel (Land)	4920-01-110-0705
68A5J1000-1	TS, Hyd Port, Electric	1730-00-129-6326

72-8001	Ind, Toxic and Combus. Gas	4920-01-112-4950
74D120012-1001	Maint Fixt, Ejn Seat	4920-01-064-3025
	Adapter Set, Tank Sealing	4920-01-048-5515
74D460008-1003		
74D460017-1001	Vlv, Reg, Fluid Press, Seal Gun	4820-01-140-3183
74D750003-1001	Adpt - Missile Cradle, AIM-7F	1450-01-112-5053
74D750004-1001	Trolley - Single Stores	1730-01-059-2802
74D750006-1002	Adapt, Hoisting - Weap Load RH	1730-01-098-5254
74D750019-1001	Trolley, Mis/LAU, Mayerick	1730-01-100-8913
74D750020-1001	Adapter, Test - Breech	4920-01-073-8196
74D750037-1001	Adapt, Test - Aux Breech	4920-01-114-8390
74D750051-1001	Adapter, Test - AIM-9 Missile System	4920-01-175-9134
	Stand Assembly (ADU-400/E)	4935-01-047-4454
787AS200		
	Tie Down, Aircraft	1730-01-008-0706
916AS100-1		

980000	AC, Air Gnd, Cond, Mobil	4120-01-017-9189
ANAWM42A	Test Set, Elec Fuzing	4920-00-138-7090
D12025-001	Pumping Unit, Hydraulic	4320-01-098-6713
DPPH100	Tester, Spring Resiliency	6635-00-578-5285
LAGANA-1	Tester, Cabin Leakage	4920-01-063-0120
M008348-1-1	Inflator Assy, Tire	6685-00-124-4336
MDA151-002	Heating Element Electrical	4920-01-152-9077
MILG8348CLASS1	Gage Press Dial Indicating	6685-00-248-6974
MILG8348CLASS1	Gage Assy Air Pressure	6685-00-506-8882
	Power Plant, Mobil Elec	6115-00-037-2005
NC-8A-1 (LAND)		
NF20-1	Breathing System	4240-01-140-5358

SUPPORT EQUIPMENT PECULIAR TO MCAIR/GD AT PATUXENT RIVER

1128AS100	Jack, Hand Hyd, 20TON	1730-01-109-1146
1182AS100-1	Tractor, A/C Towing (OV)	1740-01-069-8231
156575	Adapter, Soft Belt (Aero 64A)	1730-00-948-3532
	Test Set Firing Circuit	4920-00-152-1997
178AS100	(AN/AWM54)	
2001MC	Fluid Makeup Unit, Liq Cool	4920-01-092-7266
215-00303-50	Dolly-Multi Purpose	1730-00-133-9417
	Leak Detector, Ultrasonic	6625-00-960-5062
4918A		
	Anchor Fitting Assembly	1730-01-141-2284
534AS100-1	(HLK-279/F3)	
	Air Cylinder, Port	1730-00-625-6872
60180D1		
	Tiedown, Aircraft	1730-00-572-7370
61A101D		
61A108J1-1	Preoiler (PON 6)	4930-00-888-5119
	Service Unit, Hyd Hand Pump	1730-01-088-4611

630AS100-11		
	MEPP.ME-1A (Hangar)	6125-00-097-8327
634AS100-E1		
64A114D16-1	Aero-58A Adapter, Front	1740-00-754-4804
64A114D17-1	Aero-58A Adapter, Rear	1740-00-675-6031
64A114D322-1	Single Stores Adapter (ADU-496/E)	1730-01-174-1885
64A127J1-1	Cradle, Transport, Ej Seat	1730-00-944-5498
64A90F1	Compressor Power Unit (Land)	2835-00-923-5380
65A101D1-2	Band, Hoisting (HLK-276)	1730-01-141-2280
65A101D2-2	Band, Hoisting (HLK-277)	1730-01-141-2282
65A101D3-1	Latch Assy (HLK-278)	1730-01-141-2281
65A101H46-1	Band, Hoisting (HLK-275)	1730-01-141-2283
68A4J1000-1	TS, Hyd Port, Diesel (Land)	4920-01-110-0705
68A5J1000-1	TS, Hyd Port, Electric	1730-00-129-6326
72-8001	Ind, Toxic & Combus. Gas	4920-01-112-4950
74D110172-1001	Tool Set - Composite Repair	5180-01-163-0275
74D460017-1001	Vlv, Reg, fluid Press, Seal Gun	4820--01-140-3183
789AS920	Guided Missile Truck Adp	1730-01-088-2353

916AS100-1	Tie Down, Aircraft	1730-01-008-0706
98000	AC, Air Gnd, Cond, Mobil	4120-01-017-9189
AM-D-0-MDA1S1-101	Heat Blanket/Vac-Strct RP	4920-01-163-0274
AM-D-0-MDA1S1-103	Heat Blanket/Vac-Strct RP	4920-01-154-2758
AM-D-0-MDA1S1-105	Heat Blanket/Vac-Strct RP	4920-01-146-0257
AM-D-0-MDA1S1-107	Heat Blanket/Vac-Strct RP	4920-01-146-0258
ANAWM42A	Test Set, Elec Fuzing	4920-00-138-7090
	Pumping Unit, Hydraulic	4320-01-098-6713
D12025-001		
	Power Plan, Mobil Elec	6115-00-037-2005
NC-8A-1 (Land)		
NF20-1	Breathing System	4240-01-140-5458
	Tractor, Wheeled, A/C	1740-00-414-7150
TA75B	Towing	

ATTACHMENT 45

SECURITY IMPLEMENTATION PLAN (U)

01 DECEMBER 1987

01 DECEMBER 1987

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1 INTRODUCTION AND SUMMARY (U)

REDACTED McDonnell Aircraft Company (MCAIR) and General Dynamics Fort Worth (GDFW) shall support the purpose and objective of the Advanced Tactical Aircraft (ATA) security program. Both companies have available and shall provide the resources to satisfy the Navy's security requirements. These requirements will be enforced at every level and throughout every phase of this program. The team's primary intent shall be to deny to our adversaries any information that could be used to develop countermeasures to neutralize survivability and/or limit mission effectiveness of the ATA. The MCAIR/GDFW team shall be dedicated to the goal of providing the Navy with an ATA that is uncompromised.

1.1 (U) Security Policy

REDACTED This security implementation plan is based on guidance provided in the DD254, Contract Security Classification Specification, the H-1 clause in the contract, and the following security transition phasing for Full-Scale Engineering Development (FSED). This transition of the program from "black" to "checkerboard" (portions black, portions white) will be accomplished in phases in order to minimize disruption to the program, ensure an orderly transition, and to prevent any inadvertent disclosures. These phases are outlined further below.

Phase I - A covert compartmented program from November 1984 - November 1986.

Phase II - A compartmented program from November 1986 - January 1988.

Phase III - A "checkerboard" program from January 1988 - (TBD) which supports FSED and maintains design, performance and some technologies as compartmented but permits support, cost, schedule and other authorized technologies to be at GENSER classification levels.

Phase IIIa - An OPSEC plan specifically tailored to minimize the exposure of the ATA in FSED, starting with rollout for first flight or test.

Phase IV - A program for the operational fleet that maintains LO performance as Special Access, the aircraft as GENSER classified, and all other information at the appropriate collateral GENSER classification.

REDACTED The ATA security team shall work closely with the Navy program security officer (PSO) to direct transition from the covert demonstration/validation (DEM/VAL) phase of the contract into the FSED phase. The Navy's announcement, at FSED contract award, of the program's existence will allow some manufacturing and procurement activities to proceed in a collateral classified or unclassified environment.

1.2 (U) Security Implementation Plan

REDACTED security implementation plan addresses the phased and controlled downgrading of ATA security requirements as the program transitions through its life cycle in accordance with the following transition guidance:

1.2.1 (U) Special Access Handling:

- **REDACTED** All Low Observable (LO) parts, pieces, materials, subassemblies and business relationships.
- **REDACTED** LO manufacturing technologies and processes.
- **REDACTED** LO data, engineering specifics and design drawings.
- (U) Access to the principal manufacturing and assembly facilities.
- **REDACTED** LO data flights shall be flown only from NWC and shall require specific CNO approval. LO flight data shall be considered **REDACTED** information under a separate codeword to maintain strict need-to-know.
- (U) Mission sensitive capabilities.

1.2.2 **REDACTED** At contract award, the Navy will have announced the following:

- **REDACTED** ATA will replace A-6 **REDACTED**.
- **REDACTED** (Note - There will be no quantification of any performance factors.)
- (U) IOC will be "mid-90's".

° (U) Prime contractor team members and principal subcontractors.

° **REDACTED** [illegible]PI contract and price; teaming arrangement and competition strategy. (Note: The contract itself is classified, but the contract number is unclassified.)

1.2.3 **REDACTED** On 1 January 1988, or after contract award, whichever is later:

° **REDACTED** Subcontracts by the primes will be non-SAP at the appropriate GENSER level for all except LO items.

° **REDACTED** Advertising by all primes and authorized subcontractors if approved by the Program Office will be allowed as long as LO/stealth references are not made.

° (U) Advertising shall use a single authorized "artist's concept" of the aircraft instead of the real design.

° **REDACTED** Navy manpower and MILCON planning for ATA shall be non-SAP at the appropriate GENSER level.

° (U) The prime contractor team shall establish non-SAP program offices for advertising, marketing, personnel files, non-SAP contracts, etc.

° (U) Co-mingling of program material with DOD collateral classified material and general unclassified information will be permitted as long as strict accountability procedures for program material are maintained.

° **REDACTED** subcontracts to foreign sources will be permitted.

° (U) Co-mingling of special access programs will be authorized on a case-by-case basis.

° (U) Invoices will be approved by local plant ACO's and submitted to the PCO for payment.

1.2.4 **REDACTED** On 1 October 1988, the Navy budget submittal to OSD shall show:

° **REDACTED** FY90-94 funding/quantities and IOC as **REDACTED**.

1.2.5 (U) After rollout, an OPSEC program will include:

° (U) Close examination of the aircraft shall remain restricted and controlled in accordance with the appropriate security measures for a special access program. Government provided facilities at Government installations will include physical security systems (e.g., alarm systems, fences). The contractor will be responsible for operating and manning those security systems (e.g., guards, document control).

° (U) All aircraft will be hangared - minimum time on ramp.

° **REDACTED** ATA hangar and ramp will be protected in accordance with SAP procedures.

° (U) The "two man rule" shall apply to all contractor and government access to the aircraft.

- (U) FSED flights will be in specifically approved areas which will minimize the risk of compromise in the event of a mishap
- (U) FSED flights at non-military airfields (contractor premises) shall be on a low profile basis.
- (U) Ground operations and tests shall be within an established "exclusion area".
- (U) Test flights outside the airport traffic area shall have a chase plan.
- (U) FSED flight facilities shall have an approved mishap plan which will include a quick reaction security team for crash site perimeter control. "First on scene" is mandatory. NATC with contractor support shall prepare a water salvage plan coordinated with CINCLANTFLT.

REDACTED this plan also addresses the security requirements for Special Access Program (SAP), DoD collateral classified, and unclassified to meet the ATA Program security requirements. SAP and DoD collateral classified are defined as:

- **REDACTED** SAP compartmented material: classified material that is afforded additional protection by limiting its access to only program approved and briefed persons, and restricting its use and storage to program dedicated areas.

- **REDACTED** DoD collateral classified material: material routinely classified according to standard GENSER levels of

classification, but which does not require limited access or restricted use in addition to standard need-to-know limitations.

REDACTED this plan details the security procedures and organizational structures to meet ATA security requirements for FSED. This plan also includes a classification guide for data, parts, and hardware during FSED, the methods we will use to procure parts, the security aspects of financial transactions, and a description of our plan for secure manufacturing.

(U) Additional documents that serve as guidelines in the implementation of our security program can be found in References 1 - 10.

(U) Although not specifically addressed in a separate chapter, co-utilization or co-mingling of resources is discussed in all the chapters as they relate to the subject. The basic ground rules are that in program dedicated areas SAP, DoD collateral classified, and unclassified material can be worked together. DoD collateral classified material can be stored in program areas. In nonprogram dedicated areas SAP will neither be worked with nor stored.

2 SECURITY PHASING PLAN (U)

REDACTED This security implementation plan is based on a phased and controlled downgrading of ATA security requirements as the program transitions through its life cycle.

REDACTED Major events in the ATA program signal a significant change in activity and involvement and are natural points at which a change in security requirements, as shown in Figure 2-1 will occur.

(U) In accordance with these phased security requirements, the ATA security management system will be adjusted.

Figure 2-1 **REDACTED** ATA SECURITY PHASING

EVENT	PHASE	PHASED SECURITY REQUIREMENTS
Justification for Major System New Start	Concept Formulation	**REDACTED** SAP, Classified Mission, Technology, Schedule, Program Scope
Defense System Acquisition Review Council -Milestone I	Demonstration/ Validation	Compartmented, SAP, Classified Mission, Technology, Schedule, Program Scope
Milestone II	Full Scale Engineering Development (FSED) -Design	Multifaceted (Checkerboard). LO, Mission Sensitive Capabilities are SAP. Program funding becomes GENSER.

First Flight	FSED - Test	Same except technology revealing shape declassified
Milestone IIIA	Pilot Production	Same SAP remains for P3I
Milestone IIIB	Rate Production	TBD
Initial Operational Capability	Full Deployment	LO remains SAP Aircraft GENSER

2.1 (U) Full-Scale Engineering Development

REDACTED The PSO issued program classification guides and program security manual are revised to remove the covert requirements and acknowledge ATA program existence and the contractor team. The contractor will proceed with FSED, protecting the program through special access program administrative procedures and physical security for all items which retain the special access designation. This will allow unclassified FSED activities to be co-mingled with the other contractor business.

2.2 (U) First Flight

REDACTED The next change in security will occur as the program moves into the flight test and Navy evaluation phase. At this time, the external shape of the aircraft will be declassified, permitting the Navy and the contractor to conduct the test and evaluation

activities on a low profile visibility basis without revealing technological information. As part of the OPSEC Plan, provisions will be made to include Government supplied chase planes and quick reaction security teams to ensure "first on scene" in case of mishap. Other security measures such as exclusion areas for ground operations and tests will also be included in the OPSEC Plan.

2.3 (U) Pilot Production

REDACTED current with successful test and evaluation phases, the ATA will be approved for pilot production. Minimal special access program requirements will be required on the basic ATA program. More stringent security requirements will be imposed beginning with early preplanned product improvement (P^3I) studies. At this time, the impact will be on a limited number of personnel and activities, primarily in the engineering areas.

2.4 (U) PSO Guidance

(U) Security phasing plans depend on guidance from the PSO and are subject to approval of the PSO.

3 APPROACH AND ORGANIZATION (U)

(U) The program security organization has the authority and responsibility to ensure that the policies are strictly enforced across the entire effort.

3.1 (U) Approach

(U) There are two central policies that have affected security decisions on this program through the DEM/VAL phase

- **REDACTED** National security policy, as promulgated in ATA security guidelines, dictated the need to protect the existence of this program and its technology to maintain a technological edge on our opposition.

- (U) All program objectives, activities, data, and end products must be protected from unauthorized and/or inadvertent disclosure to any person not having program clearance and certified need-to-know.

(U) Currently all program information and activities are safeguarded with their true nature concealed from anyone without certified access to unauthorized persons from gaining access to classified information and material.

(U) With the FSED contract award announcement, the policy regarding program existence will be appropriately modified; however, the policy regarding protection of critical technology will remain in effect. The security implementation plan addresses the approach to security management during FSED under these modified policies.

(U) The approved security practices used for DEM/VAL will be continued. As FSED award, the

team will transition to a multifaceted "checkerboard" security system (SAP, DoD collateral classified, and unclassified) as described in this plan, upon approval of the PSO.

3.2 (U) Organization

REDACTED security manager and deputy, who report directly to the program managers, are responsible for security management. The principal security manager position and the deputy will be staffed at the two different principal locations of performance.

3.3 (U) Security Staff and Functions

REDACTED the program security organizations will be responsible for guiding all security actions. The program security management will be the focal point for all security interaction between the Navy Program Security Officer and the contractor.

REDACTED A facility control officer (FCO) will be selected for each of the three major facilities; St. Louis; Fort Worth; and Tulsa. FCOs will also be assigned at test sites where permanent contractor offices are established.

REDACTED The program security manager/deputy will maintain active roles in all aspects of the program. Security will monitor all elements within the program to ensure compliance with requirements of the DD254. The security standard practice procedure (SSPP), developed to satisfy program

security requirements, will be used for everyday guidance. Effective communication with the PSO on matters requiring Navy concurrence will ensure that all policy and procedural questions are resolved quickly and efficiently.

4 PHYSICAL SECURITY (U)

(U) In addition to existing corporate security measures, the ATA security team shall establish special construction, protection, and access standards to provide the necessary physical security in all program areas. In accordance with the CDRL, a Facility Security Profile will be submitted 45 days after contract award, detailing the physical plant layouts at all contractor locations.

4.1 (U) Plant Protection

REDACTED the contractor shall practice in-depth plant security. This includes fenced-in property with security patrols, guard-controlled perimeter access, and employee picture badges, supplemented where appropriate by electronic intrusion detection and area access systems.

REDACTED As the first flight date approaches, firemen at Tulsa will be accessed and trained on safety and egress from the ATA for emergency situations.

4.2 (U) Standards for Program Areas

REDACTED areas shall be approved by the Navy's program security officer, in accordance with the program security manual (PSM), DoD Industrial Security Manual (ISM), and DIAM 50-3 standards. Within 30 days after contract award, the Contractor will submit a request for the Navy to conduct a TEMPEST Vulnerability Assessment and an Instrumented TEMPEST Survey as described in the DD-254.

REDACTED GDFW program facility was evaluated for TEMPEST. It was determined that because of the large control space including the fenced company (government) property and Carswell Air Force Base, the location did not require a screen room(s) for automated data processing equipment. Such a determination is in accord with NACSIM 5004, TEMPEST Counter-measures for Facilities Within the US, issued Jan 1984 which provides for an assessment of the control space based upon the CONUS location, amount and classification level of processing, etc., with a view to requiring costly shielded facilities only where absolutely required. Therefore, screen rooms are not required. A new TEMPEST shielded program building is planned and will be located off the government property.

4.2.1 **REDACTED** Construction - All program special access areas where ATA material is stored or discussed are constructed in accordance with DIAM 50-3 to prevent unauthorized entry; visual, aural, or electronic access; or removal of program material.

Collateral classified areas shall be constructed to the ISM. The facilities used during DEM/VAL will also be used during FSED. Additional facilities or work areas will be secured to the required standards. Security plans will be forwarded to the PSO for approval prior to use.

4.2.2 **REDACTED** Access Control to Secured Program Areas - Access to all secured program areas will be controlled. Security guard posts at each secured facility or perimeter will be manned on a 24 hour-a-day, seven-day-per week basis. Card reader access controls or mechanical access devices may be used in some areas. A two-person control system will be in effect so that no one person can have access to the facility at any time. An unclassified master access roster shall be maintained at facility entry points and a program-specific badging system shall be in effect. MCAIR, GDFW, and selected subcontractor personnel are included on each others' master access list.

4.2.3 (U) Intrusion Detection - Program areas will be protected by high security alarms that meet the standards of DIAM 50-3, Chapter 3. Twenty-four hour monitoring of alarms will be provided. Guard personnel will respond to an alarm within five minutes or less (three minutes for approved open storage areas). Additional guards shall be available to assist the responding guards in an emergency.

4.2.4 (U) Telephones - All program areas will be equipped with a telephone system approved by the PSO.

4.2.5 (U) Automated Information Systems (AIS) Equipment - AIS equipment used within the program secured areas is evaluated for TEMPEST vulnerability. Appropriate TEMPEST countermeasures and controls are applied based on risk assessment in coordination with the program security office. See Section 12 for further guidance.

4.2.6 (U) Test Facilities - Physical and operational security for tests requiring special access protection will be accomplished in compliance with the PSM or specific direction from the PSO. Plans for these tests will be prepared and submitted to the PSO for approval. A flight and ground test operational security (OPSEC) plan will be developed in accordance with the CDRL to cover both security and technical issues. Lists of program-accessed personnel, area access controls, and extensive pre-test and post-test area checks are included in the plan to ensure that no program material is left behind. During testing, program security requirements are imposed and the test area is closed to all but program personnel. Classified test material and classified information will be under constant surveillance of two program accessed personnel. Transportation of material and data from remote sites shall be in accordance with an approved Transportation Plan.

(U) For tests at government facilities, the FCO will work closely with the PSO to ensure that a complete, comprehensive test security plan is developed and agreed to by all parties.

(U) Tests at subcontractor facilities, just as those conducted by the ATA team, will be conducted in full compliance with a test security plan which has been approved by the PSO.

4.2.7 (U) Subcontractor Facilities - Subcontractor facilities which are required under the purview of the special access controls will be nominated, inspected, and accredited by direction of the PSO.

5 DOCUMENT SECURITY (U)

(U) This plan covers accountability, marking, storage, inventory, transmission, reproduction, and destruction. Classified program documents shall be safeguarded, controlled, and transmitted in accordance with the program security manual. GENSER classified documents will be afforded normal protection in accordance with content. Care will be taken to ensure that a compilation of unclassified material does not reveal program classified information.

REDACTED The contractor shall maintain complete accountability records and receipts showing the current disposition (i.e., origination, transmittal, reproduction, regrading, internal accountability, and destruction) of all SAP classified documents. These records are maintained separate from normal DoD accountability records, within the program area. The accountability system is described in detail in the contractor's Security Standard Practice Procedure (SSPP). Subcontractors are required to maintain the

same separate but parallel accountability system, with the same adherence to PSM.

5.1 (U) Accountability

(U) All SAP classified (SECRET, TOP SECRET) documents received, produced by, or in the possession of the program shall be controlled under provisions of the program classification manual. Some material previously classified may be declassified consistent with the FSED classification guide issued by the PSO. That material may be extracted from the controlled document and used in the unclassified environment, after PSO approval.

5.2 (U) Marking/Storage

(U) All program classified data shall be conspicuously marked with appropriate program classification labels or cover sheets. All classified documents shall be marked at the time of creation in accordance with applicable security classification guides.

(U) Storage within program areas will be in approved containers or in areas approved for open storage. Storage outside the program controlled areas will be only under conditions approved in advance by the PSO. GSA approved containers (Class VI) are designated in the Program Security Manual for Program use. Filing cabinets secured by lock bars and Sargent and Greenleaf 3-position changeable combination padlocks are in use at some facilities and are approved for storage of Level III materials

excluding magnetic media. Lock bar containers in use at the contract award are authorized.

5.3 (U) Document Control

REDACTED A control station shall be operated at each location by specially trained Contractor employees. Automated document accountability systems along with periodic inventories shall be used to maintain accurate records of classified documents. Destruction/disposition of documents no longer required shall keep the volume of classified documents at a manageable level. Random monthly inventories shall be accomplished to sample the accuracy of the accountability system. A 100 percent inventory is conducted annually. This inventory will attest that inactive document control log entries for destroyed or transferred material have been verified by sighting of transmittal or destruction receipt. This inactive entry verification will be accomplished throughout the current year and need not be repeated for entries verified and attested to in previous audits. Any unresolved discrepancies noted during the audit will be reported as part of the annual inventory report.

5.4 (U) Transmission Methods

(U) Classified data up through SECRET shall be transmitted by registered U.S. mail, by approved courier, by secure government data communication (DACOM) system, or by secure government data link. TOP SECRET data is transmitted by secure data communication or by approved courier. A

secure communication link between the government, the prime contractors, and subcontractors is planned for the ATA program. Subcontractors that will manufacture and produce SAP parts in SAP facilities will require secure communications. The estimate of suppliers who would have SAP facilities is less than 40 suppliers. .

(U) SECRET data transmitted by mail shall be sent registered mail return receipt required. Procedures for maintaining security for this method (detailed in SSPP and below) include multiple wrappings, sterile addresses, and two-person escort between the sterile address and program area. SECRET documents may be transported on commercial flights by two authorized couriers. Notification of the movement of SECRET material shall be made to the FCO in advance.

(U) Movement of TOP SECRET data by courier on military aircraft, or dedicated contractor aircraft shall be approved in advance by the PSO, and the two-person escort rule applies.

REDACTED All compartmented correspondence relating to this contract and its administration shall be no less than **REDACTED**. Deliverables and all other documentation shall be classified as governed by the DD-254 and this attachment 45. Transmission (i.e., mail/handcarry) of **REDACTED** documents outside of the secure facility shall be in double-wrapped opaque sealed containers. The inner envelope or container shall be marked with the highest classification of the contents and the letter

"B" in large red block letters, placed in the upper right-hand corner of the envelope and shall be marked "TO BE OPENED BY ADDRESSEE ONLY" and both the addressee's and addressor's secure P.O. box shall appear on the front of the envelope with the following phrase centered beneath:

THIS PACKAGE CONTAINS CLASSIFIED U.S. GOVERNMENT INFORMATION. IF FOUND, PLEASE DO NOT OPEN. CALL ONE OF THE FOLLOWING NUMBERS COLLECT:

REDACTED

For SECRET material, the inner envelope shall contain a receipt form/card which identifies the originator and address as well as the serial number, date and copy number of the correspondence contained therein. The plain outer envelope will be addressed post-office box to post-office box. using designated boxholder's names; material will be sent registered/return receipt requested. In no case shall the Contractor's name or logo appear on any envelope. Postage meter machines shall not be used. TOP SECRET correspondence shall be handled via Armed Forces Courier Service (ARFCOS) when time permits. Otherwise, TOP SECRET material will be handled by two specifically designated program-indoctrinated couriers, or shall be transmitted via secure (encrypted) DACOM transmission, if available. TOP SECRET may not under any circumstances be mailed through the postal system. The Contractors will immediately inform both the

PCO and the PSO of any change in either Post Office Box Number or in boxholder's name.

Envelopes and addresses for U.S. mail should be as follows:

MAIL TO BE SENT TO THE CONTRACTOR:

General Dynamics Corporation
Fort Worth, TX 76108

REDACTED

01 DECEMBER 1987

MAIL TO BE SENT TO THE PROGRAM SECURITY OFFICER

REDACTED

MAIL TO BE SENT TO THE PROGRAM MANAGER

REDACTED

(U) Non-SAP classified material is transmitted in accordance with appropriate GENSER procedures.

5.5 (U) Reproduction

(U) Reproduction of program material shall be controlled. All copier machines have access-protect devices or are controlled by security to prevent unauthorized use.

5.6 (U) Destruction

(U) Destruction techniques for classified documents include GSA-approved cross-cut shredders and heavy duty-dry disintegrators. This equipment is approved for destroying documents through the level of TOP SECRET. Shredded residue is then disposed of through the contractor disposal system.

(U) Hardware will be destroyed in accordance with instructions provided by the PSO. Those materials that cannot be destroyed in accordance with PSO instructions will be stored until the PSO removes it for his destruction.

(U) Detailed procedures for destruction are described in the SSPP.

(U) Other methods used and approved by the Government are degaussers for erasing automated data processing magnetic storage media and/or chemical decomposition.

(U) Certificates of destruction for accountable classified material shall be signed by two program briefed employees at the time of actual destruction.

6 PROGRAM ACCESS CONTROLS (U)

REDACTED access to program classified material and information shall be restricted to personnel who have the proper clearance, have a certified need-to-know, have been approved by the PSO and have been

briefed on program security rules. The program access request (PAR) systems shall be used.

6.1 (U) Program Personnel

(U) All requests for Level 3 and Level 4 access will be recommended by authorized contractor personnel. Access requests will be forwarded to the program security officer for final adjudication.

(U) Only personnel with a "Need-to-Know" shall be nominated for Level 3 and 4 program access. Each nominee must possess a final SECRET clearance for Level 3 consideration and a final TOP SECRET clearance for Level 4. A PAR with detailed justification shall be submitted to the access administrator, an appointed government agent, who reviews the documentation and forwards the request to the program manager for approval. Written approval is required from the PSO for a person to be briefed into the program.

(U) Briefings shall cover physical and personnel security controls for the program and support services areas, special security controls for the special categories of classified program material, and special regulations concerning public release and export control of both classified and unclassified information and technology. Briefings and debriefings shall be conducted by designated security personnel with written acknowledgement of each briefing retained. Annual reindoctrination is performed and documented.

6.2 (U) Program Briefed Visitors

(U) Maintaining "Need-to-Know" and verification of the approved visitor's level of access is required. The hosting representative is responsible for ensuring that only the appropriate level of classified information is disclosed to the visitor.

6.3 (U) Nonprogram Briefed Visitors

(U) Those individuals not program briefed but requiring temporary access to a program area shall register their entry in a log and be under the constant supervision of a program briefed escort. This escort will make the proper announcements so program personnel can take the necessary protective measures to ensure nonexposure of program material.

6.4 (U) Security Education

REDACTED Frequent security education is the key to maintaining employees' awareness of their responsibilities for safeguarding program information as well as identifying espionage indicators. The contractor shall provide a security education program directed at teaching proper procedures, operations security, communication security, counterintelligence awareness, and the need to report all possible intelligence related contacts. This program shall be supplemented by the contractor security programs that reinforce overall security awareness. As a minimum all program personnel shall receive an annual reindoctrination

briefing. This is supplemented with topical briefings and security bulletins.

6.5 (U) Subcontractor Personnel

REDACTED contractor program access requests will be recommended by authorized contractor personnel to the PSO for approval. Personnel of new subcontractors will be initially briefed at the contractor's site by a subcontractor security representative. Subsequent personnel of that subcontractor, approved for access, may be briefed at the subcontractor's plant by subcontractor security representatives, following facility approval. In each case, the briefed personnel will be responsible for complying with the provisions of the program security manual.

7 CLASSIFICATION MANAGEMENT (U)

REDACTED classifications are assigned by the Navy. Classification guidance is based on the Level 3, Level 4, and additional classification guides. Any classification change will be approved by the original classification authority and provided in the revised security classification guide (SCG). A Classification Guide for FSED is included as Appendix A and is in accordance with the security phasing plan.

7.1 (U) Hardware Classification

(U) Listed below are the major system/structural items that will be classified.

- (U) Aircraft
- (U) Radar antenna
- (U) Nose assembly
- (U) Forward fuselage assembly
- (U) Center body assembly
- (U) Outer center body assemblies
- (U) Aft carry through section assembly
- (U) Outer wing assemblies
- (U) Upper surface skins
- (U) Lower surface skins
- (U) Structural components (LO or mission revealing)
- (U) Nozzles
- (U) Leading edges
- (U) Trailing edges
- (U) Canopy

° (U) Transparencies (when treated for LO)

(U) All major assemblies through first flight are classified special access. Fabrication of major assembly tooling is classified "special access." Details of major assembly tolls will be unclassified if shape of aircraft is not revealed. Any part or assembly that contains special access materials will be classified "special access" at the point these materials are incorporated. A tool or part will be classified "special access" if the shape of the ATA can be interpreted to reveal **REDACTED** design details or when it contains special access classified **REDACTED**.

7.2 (U) Unclassified Components

(U) Parts, tools, and materials that do not identify unique characteristics of the ATA will be unclassified. This will include conventional aircraft inventory items such as nuts and bolts, raw material, system components, and structures.

7.3 (U) Technical and Administrative Data

(U) Classification of technical and administrative data will be in accordance with the SCG, as issued and maintained by the PSO.

8 MANUFACTURING SECURITY (U)

REDACTED The security implementation plan for manufacturing activity is designed to ensure security for classified information and hardware and to allow

unclassified information and hardware be produced and stored in an unclassified environment. Care will be taken to ensure that a compilation of drawings will not reveal any classified information. This will be accomplished by:

- (U) Manufacturing of SAP classified parts in dedicated facilities

- (U) Development of numerical control (NC) parts program for SAP classified parts in program secure areas

- (U) Identification of classification of the part/ tool on the work order.

- (U) Fabrication of GENSER parts and tooling using nonprogram cleared personnel and areas

- (U) Release of GENSER drawings to the open shop without next assembly information

8.1 (U) Manufacturing Planning

(U) All manufacturing planning for classified parts will be accomplished in appropriate secure areas. Manufacturing planning for unclassified parts will be prepared using current unclassified procedures and areas. Classification of parts and the tools necessary to manufacture them will be verified by program cleared manufacturing management personnel. A security specialist will be available to

assist manufacturing planning in determining proper classification.

(U) Planning for classified parts will be classified and will contain appropriate work instructions defining the steps required to protect program security while manufacturing and handling the part.

(U) Planning (work orders/work instructions) for unclassified parts will be produced so that uncleared personnel may utilize unclassified planning and drawings in unsecured areas to manufacture the part, without risk of disclosure of any classified or sensitive program data.

8.2 (U) Tool Design

(U) Tool design personnel assigned to the program will be briefed and located in program secure areas. The classification of a tool design will be the same as the classification of the parts or assembly it produces. If any details of a classified tool can be fabricated as unclassified, they will be so noted on the classified tool design by the tool designer. If any tool detail is classified, the assembled tool will be classified. The contractor security specialist will ensure that all tool design drawings are properly classified.

(U) Classified tool designs will be treated as controlled documents and will be handled only by program cleared personnel in program secured facilities.

(U) Unclassified tool designs will be released using the current unclassified procedures. Prior to an unclassified tool design release, designs will be reviewed by the security specialist to ensure that classified information is not disclosed.

(U) NC tool designs will be accomplished on program secured CAD/CAM terminals for classified tools. To provide secure data communication to NC machines for classified tools, machine control data will be transmitted to secured manufacturing areas either via encrypted data lines or be hand-carried according to approved procedures. Unclassified NC tapes/floppies will be made for unclassified tool designs and run on unsecured machines using existing production procedures. A verification system will be devised to ensure only unclassified material is on the tape/floppy.

8.3 (U) Tool Fabrication

(U) All tool manufacturing activity, including rework and maintenance, will be accomplished by existing tool manufacturing functions. Tools that reveal any of the classified characteristics of the part they make will be classified and controlled in the accountability system. Assignment of a security classification to tools will be the responsibility of a program security specialist.

(U) When a tool is unclassified, tool fabrication efforts will be accomplished using existing unsecured facilities, machines, and data systems by nonprogram cleared personnel.

(U) Classified tools will be fabricated by program cleared personnel in program secured facilities. All aspects of the fabrication effort will be controlled.

8.4 (U) Detail Parts Fabrication

(U) Classified parts will be fabricated by program cleared personnel in program secured areas. Handling of NC data for parts fabrication will be accomplished in the same manner as in handling NC tool designs. Unclassified parts will be handled in the normal production manner.

(U) Fabrication of wire harnesses and tubing will be performed in the regular electrical and tubing shops by non-program cleared personnel. No classified information will be released to the wire harness or tube fabrication shops. Liaison problems will be resolved through program cleared personnel when they involve the electronic development fixture.

8.5 (U) Subassembly

(U) Subassembly will be accomplished in areas consistent with classification requirements, i.e., classified subassemblies in secured areas by program cleared personnel, unclassified subassemblies in non-program areas.

8.6 (U) Major Assembly

(U) Major assembly efforts will be performed in secured areas with program cleared personnel.

8.7 (U) Final Assembly

REDACTED Final assembly, mate/splice through flight preparations will be accomplished in program secured facilities.

8.8 (U) Production Control and Scheduling

(U) Production control and shop scheduling functions for classified parts and secured manufacturing areas will be performed by program cleared personnel using procedures similar to existing operating procedures, within security requirements. These functions will be performed within program secured areas.

(U) Non-program cleared personnel performing production control and shop scheduling functions in non-program areas on unclassified parts will continue to perform those functions with existing procedures.

8.9 (U) Classified Hardware Controls

(U) Classified hardware will be handled and controlled in accordance with the PSM. Hardware classified as special access material will only be manufactured and stored within secure program areas. Manufacturing processes wherein unclassified raw materials become classified parts or tools will be accomplished within secure areas. Partially completed parts and tools will be controlled as classified work-in-progress and properly safeguarded. Collateral classified will be handled

within approved DoD storage areas. When manufacturing processes or tests cannot be accomplished within dedicated program secure areas, screens, barriers or other types of enclosures will be used to restrict visual access and guards will be used, if necessary. In all cases a procedure will be established and approved by the PSO.

(U) Hardware classified SECRET and TOP SECRET will be accountable and controlled similar to documents. Hardware control stations will be established in the manufacturing, receiving, and assembly areas. Classified parts and tools will be identified, marked and made accountable as soon as they are completed. Classification marking will be affixed by stencil, etch, stamp, tag or other appropriate method so that the part or assembly is tracked as it proceeds in the manufacturing and assembly process. A hardware control system will be used so that as classified parts are incorporated into the total ATA the accountability of parts will be clearly tracked and adjusted as the aircraft are completed.

(U) Classified hardware will be produced and delivered by subcontractors in accordance with instructions included in their purchase orders. The purchase order will include all documentation, specifications, quantities, and a block of serial numbers to coincide with the quantities required. Subsequent purchase orders will contain the same data and a new block of serial numbers. The purchase order will also include the shipping instructions for classified hardware.

(U) Each subcontractor producing, delivering or receiving classified hardware will also have a hardware control center. At the time hardware is ready for shipment, a classified material transfer receipt will be prepared and placed inside the container with the hardware or handcarried by program couriers. The classified transfer receipt will then be used to maintain accountability and traceability of the classified parts and components as they proceed through assembly of the aircraft.

(U) As classified parts and components are incorporated into subassemblies towards the final permanent assembly, hardware control will track all movement by receipts, logs, tags, and the hardware control system.

(U) Accountability will be enhanced and confirmed by periodic inventories, audits and spot checks, in addition to an annual inventory. The importance of maintaining accurate accountability will be reinforced by a formal security education program.

(U) All classified components, assemblies, and test aircraft will be safeguarded within secure program facilities.

(U) As the aircraft are delivered a new classified transfer receipt will be prepared to control the end item. The aircraft or test article will be delivered or moved to the government test range by procedures approved by the PSO with careful attention to operations security.

8.10(U) Manufacturing Support and Test Equipment

(U) Manufacturing support and test equipment will be designed and manufactured in a manner similar to that for tools, although specific manufacturing facilities and personnel may be different. The same security criteria will be applied to these items as is applied to tools.

8.11(U) Secure Transportation

REDACTED Existing PSO approved transportation security plans will be used during FSED. In addition, existing transportation means (public carriers and company-owned intra-and inter-plant resources) will be used to transport GENSER hardware (material, parts, systems, and assemblies). An FSED transportation security plan for material and hardware will be developed and submitted to the PSO for approval. The movement of hardware and material will be between subcontractor locations, St. Louis, Fort Worth, Tulsa, and major test locations -- the Naval Air Test Center (NATC), Patuxent River, Md., and Naval Weapons Center (NWC), China Lake, Ca. The method for handling movement of SAP classified hardware between any of these locations will be included in this plan. Whenever a one-time movement of a major piece of hardware is required, specific supplements to the transportation security plan will be prepared and submitted to the PSO for approval. .

(U) All SAP classified parts or material that must be transported either between secured areas or between companies will be handled under prescribed security requirements and will be escorted by two individuals cleared for program access.

REDACTED parts or assemblies which reveal a classified view will be covered, packaged or wrapped to ensure that shape or configuration is concealed. Outer markings will be constructed so as to not reveal any association with the ATA program.

8.12 (U) Data Systems

(U) SAP manufacturing information such as automated planning, scheduling, and generation of work packages will be processed on secure computer systems. These systems will process classified data, with absolutely no connection to the normal unclassified company data systems. Access will be by program briefed personnel with terminals in program cleared facilities. System description documents detail the security protections necessary to operate in the special access environment.

(U) Existing data systems will be used for unclassified work. Separate terminals outside the SAP secured areas will be used to access these systems.

REDACTED co-mingling of SAP program and DoD collateral assets will be conducted consistent with the policy defined in this plan and Attachment 24 to the contract. Exchange of data between program

and nonprogram computers to implement this policy will be accomplished using PSO approved safeguards.

9 SECURITY ASPECTS OF PARTS PROCUREMENTE PLAN (U)

(U) A subcontracting and purchasing methodology that provides the level of security necessary to protect program classified information, parts or material will be used during FSED for SAP classified procurements.

(U) On the basis of security classification discussions in Section 7, all subcontractors/vendors will be in one of three categories:

- **REDACTED** Category A: Those companies requiring SAP personnel and facility clearances. These companies manufacture systems or components that reveal mission sensitive capabilities or signature reduction design details of ATA and therefore must be SAP classified. Examples are radar absorbing structure, radar antenna, external parts revealing aircraft shape, etc. All aspects of the relationship between the prime contractor and Category A suppliers that in any way reveals the LO nature or mission sensitive capabilities of the ATA shall be protected via SAP security procedures.

- **REDACTED** Category B: Those companies requiring SAP personnel clearances only.

These companies manufacture systems or components that do not reveal mission sensitive capabilities. However, the subcontractor personnel require access to aircraft data at the contractor's special access facilities to provide a correct interface. Examples are weapons, flight control computers, air data systems, etc. These systems or components are unclassified or classified (non-SAP) at standard DoD classifications.

° **REDACTED** Category C: Those companies not requiring SAP personnel or facility clearances. These companies manufacture systems or components that do not reveal the mission sensitive capabilities of ATA. This category includes all systems, components and parts not included in Categories A and B. Examples are raw materials, standard parts, adhesives, paint, primer and all non-revealing system components and parts for all systems. These components and parts will be unclassified although some may be classified (non-SAP) at standard DoD classifications.

9.1 (U) Subcontractor Security

REDACTED The contractor's subcontractor security personnel will provide security guidance to all subcontractors with access to classified ATA information. These vendors are required to provide security controls as specified in the PSM, DD254, and the section H clause. All subcontractors must

deal directly with the contractor, as stated in the DD254.

(U) Subcontractor security is charged with the responsibility for the following:

- (U) Conduct initial program security indoctrinations and presentation of security requirements to all approved potential subcontractors. The presentation will include, but not be limited to, current program security manual requirements and facility physical security requirements necessary to safeguard classified documents, material and information.

- (U) Advise on the construction requirements regarding alarm systems, wall hardness, sound attenuation, storage containers, as well as program security administration, locks, and locking devices in preparation for accreditation of their facility. Particular emphasis is placed on education during the initial briefings to ensure key subcontractor personnel understand the security requirements of the program.

- (U) Assist in the accreditation inspection, do follow-up assistance visits, offer advice and guidance as required. Perform formal on-site semiannual inspections of the subcontractor's administrative and physical security procedures for safeguarding the program and

may assist with the customer's required inspections.

- (U) Process subcontract/supplier initial contact information forms from accredited vendors for potential tiered subcontractors, for obtaining building convenience codes (building numbers).

9.2 (U) Subcontractor Clearance

REDACTED Subcontractors' personnel access requests will be processed through MCAIR or GDFW prior to submitting them to the PSO for approval.

9.3 (U) Procurement of Classified Items

REDACTED two methods are being used to supply RFPs to potential subcontractors for classified procurements. Potential subcontractors who have approved secured facilities will receive the RFP at their facility through registered mail. All others must have program briefed personnel prepare the subcontractor's proposal in the secured facilities of MCAIR or GDFW.

9.4 (U) Transportation

REDACTED king firms shall have DoD facility clearances and drivers and relief drivers possessing DoD SECRET clearances on all classified shipments. The contractor may also have cleared personnel who will use contractor equipment to move classified items or material. Program cleared couriers will

accompany all classified shipments, whether by truck, contractor aircraft, chartered aircraft, or commercial air carriers.

REDACTED lateral classified material and unclassified will be shipped through existing contractor channels.

9.5 (U) Receiving Inspection

(U) Classified items will be transported as specified above into cleared facilities where they will be inspected. Items that are unacceptable will be placed in a secured material review board crib and destroyed or disposed of in accordance with instructions from the contracting officer or PSO. Classified inspection records will be maintained on appropriately classified data bases on approved stand alone personal computers, controlled by Quality department in a secured area. Source inspection shall be stipulated on the purchase order if classified technical data is required. Receiving inspection will use existing receiving inspection operational procedures at each facility for unclassified items.

9.6 (U) Warehousing

REDACTED SAP classified items or material will be received at secured warehouses in St. Louis, Fort Worth, and Tulsa for processing and storage. Shipping receipts and records of classified items and material will be maintained by the warehouse custodian. The custodian will obtain a receipt for all

classified hardware released to the subassembly, final assembly or other program activity. Hardware control systems described in Section 8.9 will be utilized to track hardware accountability.

REDACTED lateral classified and unclassified material will be received **REDACTED** the existing receiving functions and processed in accordance with established procedures of each team member.

10 SECURITY ADMINISTRATION OF CONTRACTUAL AND FINANCIAL MATTERS (U)

REDACTED contractual and financial administration will be performed through the use of existing contractor systems. The procurement system provides for contracting to be accomplished as dedicated SAP classified, collateral classified, or unclassified. The type of contracting channel to be utilized will depend on the classification of the item or service procured and the classification of the information that must be provided to the vendor.

(U) Collateral classified and unclassified contracting methods shall allow the contractor to maintain the required security level without disclosure of classified information to organizations and personnel who perform unclassified contract services or provide parts. These contracting procedures shall prevent disclosure of classified information and allow for the procurement to be accomplished in the most economical manner.

(U) Payments to collateral classified and unclassified suppliers may be handled through the existing invoice payment system in accordance with the following:

- (U) Classified purchase orders and supplier invoices will be retained in a secure area.

- (U) Purchase order commitment data will be established in the unclassified environment which involves suppliers for which the contractor has placed other purchase orders. Subject data will include only supplier name, P.O. number, commitment values by Purchase Order line item, and cost charge number not traceable to the program.

- (U) As Procurement personnel in the secure area receive the supplier invoices relative to the above, they will issue a check request with proper approvals, and forward for processing payment, releasing only the data above.

REDACTED total program financial data (FSED and production lots) shall be **REDACTED**. For internal/external financial forecasting purposes that Contractor shall not disclose any total program financial data as ATA program related. Total program financial data will be fragmented by production lots so that non-cleared personnel cannot determine the total program value or lot build-up. Only the program offices shall maintain the necessary information to permit aggregation of the total program value. Combined MCAIR/GDFW

FSED financial data shall be **REDACTED** MCAIR or GDFW financial data when separated shall be unclassified. The separated financial data shall not be specifically or implicitly identifiable as ATA financial data.

11 FACILITIES (U)

(U) All SAP classified parts and tools will be fabricated, assembled, and tested in secured areas. GENSER classified and unclassified parts will be fabricated in manufacturing areas equipped with the necessary security safeguards.

12 AUTOMATED INFORMATION SYSTEMS (AIS) (U)

REDACTED The standards utilized to establish the security criteria for AIS facilities are DIAMs 50-3, 50-4, 50-5 Volume I and Volume II, and the PSM. TEMPEST standards shall be met by utilizing one or a combination of the following: RF-shielded enclosure, TEMPEST-approved equipment, selected NACSIM 5203 RED/BLACK engineering criteria, or by meeting program physical control space requirements. Future computer systems utilized to process classified data will meet the same security standards and SPPs for AISs will be submitted to the program security officer for approval.

REDACTED The contractor shall extend computer coverage to additional secure areas for the FSED phase through expansion of the encrypted data communications network. This will be accomplished

via encrypted data lines between the secured computers and workstations within secured areas in outlying buildings or remote locations. Dedicated computers and data networks will be secured and encrypted at any point where they penetrate the program secured areas.

REDACTED encrypted communication will be used between contractor sites, **REDACTED** Washington, DC, NATC- Patuxent River, NWC-China Lake, and major subcontractor locations (e.g., engine, radar).

REDACTED all classified data transmissions, which traverse uncleared facilities, will be encrypted by government furnished cryptographic equipment or transmission lines will be physically secured and approved by the PSO. All encryption will be accomplished with Navy-provided keying material supplied by the National Security Agency and classified at the same level as, or higher than, the classification of the data being transmitted.

REDACTED extensive internal and external secure communications network for the transmission of classified voice and data program material will be utilized. The internal system will be room to room or building to building through varying areas of physical protection. The external system will be site to site, i.e., St. Louis to Tulsa, Fort Worth to Washington D.C. Government furnished equipment for encryption will be required to implement this network.

REDACTED The contractor will comply with the 2-person rule during all processing/occupancy times to protect SAP material. The number of hours per day that any computer will operate depends on the workload. Unattended after hour computing will only be allowed when approved by the PSO.

(U) REFERENCES

1. (U) Dod Dir 5240.6 Counterintelligence Awareness and Briefing Program

2. (U) DoD 5220.22M, Industrial Security Manual for Safeguarding Classified Information

3. (U) DoD 5200.1R/OPNAVINST 5510.1 G, Information Security Program Regulations

4. (U) DIAM 50-3, Physical Security Standards for Sensitive Compartmented Information Facilities

5. (U) DIAM 50-4B, Security of Compartmented Computer Operations

6. (U) DIAM 50-5, Vol I and II, Sensitive Compartmented Information Contractor Administrative Security

7. (U) NACSIM 5004, TEMPEST Countermeasures for Facilities within the US

8. (U) NACSIM 5201, TEMPEST Guidelines for Equipment/System Design Installations

9. (U) NACSIM 5203, Guidelines for Facility Design and Red/Black Installations

10. (U) NACSIM 5204, Shielded Enclosures

TITLE 48--Federal Acquisition Regulations System
Chapter 1
Subchapter H--Clauses and Forms
Part 52--Solicitation Provisions and Contract Clauses
Subpart 52.2--Texts of Provisions and Clauses
§ 52.219

§ 52.249-2 Termination for Convenience of the Government (Fixed-Price).

As prescribed in 49.502(b)(1)(i), insert the following clause in solicitations and contracts when a fixed-price contract is contemplated, and the contract amount is expected to be over $100,000, except in contracts for (a) dismantling and demolition, (b) research and development work with an educational or nonprofit institution on a no-profit basis, or (c) architect-engineer services. It shall not be used if the clause at 52.249-4, Termination for Convenience of the Government (Services) (Short Form), is appropriate (see 49.502(c)), or one of the clauses prescribed or cited at 49.505(a), (b), or (e), is appropriate.

TERMINATION FOR CONVENIENCE OF THE GOVERNMENT (FIXED-PRICE) (APR 1984)

(a) The Government may terminate performance of work under this contract in whole or, from time to time, in part if the Contracting Officer determines that a termination is in the Government's interest. The Contracting Officer shall terminate by delivering

to the Contractor a Notice of Termination specifying the extent of termination and the effective date.

(b) After receipt of a Notice of Termination, and except as directed by the Contracting Officer, the Contractor shall immediately proceed with the following obligations, regardless of any delay in determining or adjusting any amounts due under this clause:

(1) Stop work as specified in the notice.

(2) Place no further subcontracts or orders (referred to as subcontracts in this clause) for materials, services, or facilities, except as necessary to complete the continued portion of the contract.

(3) Terminate all subcontracts to the extent they relate to the work terminated.

(4) Assign to the Government, as directed by the Contracting Officer, all right, title, and interest of the Contractor under the subcontracts terminated, in which case the Government shall have the right to settle or to pay any termination settlement proposal arising out of those terminations.

(5) With approval or ratification to the extent required by the Contracting Officer, settle all outstanding liabilities and termination settlement proposals arising from the termination

of subcontracts; the approval or ratification will be final for purposes of this clause.

(6) As directed by the Contracting Officer, transfer title and deliver to the Government (i) the fabricated or unfabricated parts, work in process, completed work, supplies, and other material produced or acquired for the work terminated, and (ii) the completed or partially completed plans, drawings, information, and other property that, if the contract had been completed, would be required to be furnished to the Government.

(7) Complete performance of the work not terminated.

(8) Take any action that may be necessary, or that the Contracting Officer may direct, for the protection and preservation of the property related to this contract that is in the possession of the Contractor and in which the Government has or may acquire an interest.

(9) Use its best efforts to sell, as directed or authorized by the Contracting Officer, any property of the types referred to in subparagraph (6) above; provided, however, that the Contractor (i) is not required to extend credit to any purchaser and (ii) may acquire the property under the conditions prescribed by, and at prices approved by, the Contracting Officer. The proceeds of any transfer or disposition will be

applied to reduce any payments to be made by the Government under this contract, credited to the price or cost of the work, or paid in any other manner directed by the Contracting Officer.

(c) After expiration of the plant clearance period as defined in Subpart 45.6 of the Federal Acquisition Regulation, the Contractor may submit to the Contracting Officer a list, certified as to quantity and quality, of termination inventory not previously disposed of, excluding items authorized for disposition by the Contracting Officer. The Contractor may request the Government to remove those items or enter into an agreement for their storage. Within 15 days, the Government will accept title to those items and remove them or enter into a storage agreement. The Contracting Officer may verify the list upon removal of the items, or if stored, within 45 days from submission of the list, and shall correct the list, as necessary, before final settlement.

(d) After termination, the Contractor shall submit a final termination settlement proposal to the Contracting Officer in the form and with the certification prescribed by the Contracting Officer. The Contractor shall submit the proposal promptly, but no later than 1 year from the effective date of termination, unless extended in writing by the Contracting Officer upon written request of the Contractor within this 1-year period. However, if the Contracting Officer determines that the facts justify it, a termination settlement proposal may be received and acted on after 1 year or any extension.

If the Contractor fails to submit the proposal within the time allowed, the Contracting Officer may determine, on the basis of information available, the amount, if any, due the Contractor because of the termination and shall pay the amount determined.

(e) Subject to paragraph (d) above, the Contractor and the Contracting Officer may agree upon the whole or any part of the amount to be paid because of the termination. The amount may include a reasonable allowance for profit on work done. However, the agreed amount, whether under this paragraph (e) or paragraph (f) below, exclusive of costs shown in subparagraph (f)(3) below, may not exceed the total contract price as reduced by (a) the amount of payments previously made and (2) the contract price of work not terminated. The contract shall be amended, and the Contractor paid the agreed amount. Paragraph (f) below shall not limit, restrict, or affect the amount that may be agreed upon to be paid under this paragraph.

(f) If the Contractor and the Contracting Officer fail to agree on the whole amount to be paid because of the termination of work, the Contracting Officer shall pay the Contractor the amounts determined by the Contracting Officer as follows, but without duplication of any amounts agreed on under paragraph (e) above:

(1) The contract price for completed supplies or services accepted by the Government (or sold or acquired under subparagraph (b)(9) above) not

previously paid for, adjusted for any saving of freight and other charges.

(2) The total of—

(i) The costs incurred in the performance of the work terminated, including initial costs and preparatory expense allocable thereto, but excluding any costs attributable to supplies or services paid or to be paid under subparagraph (f)(1) above;

(ii) The cost of settling and paying termination settlement proposals under terminated subcontracts that are properly chargeable to the terminated portion of the contract if not included in subdivision (i) above; and

(iii) A sum, as profit on subdivision (i) above, determined by the Contracting Officer under 49.202 of the Federal Acquisition Regulation, in effect on the date of this contract, to be fair and reasonable; however, if it appears that the Contractor would have sustained a loss on the entire contract had it been completed, the Contracting Officer shall allow no profit under this subdivision (iii) and shall reduce the settlement to reflect the indicated rate of loss.

(3) The reasonable costs of settlement of the work terminated, including

(i) Accounting, legal, clerical, and other

expenses reasonably necessary for the preparation of termination settlement proposals and supporting data;

(ii) The termination and settlement of subcontracts (excluding the amounts of such settlements); and

(iii) Storage, transportation, and other costs incurred, reasonably necessary for the preservation, protection, or disposition of the termination inventory.

(g) Except for normal spoilage, and except to the extent that the Government expressly assumed the risk of loss, the Contracting Officer shall exclude from the amounts payable to the Contractor under paragraph (f) above, the fair value, as determined by the Contracting Officer, of property that is destroyed, lost, stolen, or damaged so as to become undeliverable to the Government or to a buyer.

(h) The cost principles and procedures of Part 31 of the Federal Acquisition Regulation, in effect on the date of this contract, shall govern all costs claimed, agreed to, or determined under this clause.

(i) The Contractor shall have the right of appeal, under the Disputes clause, from any determination made by the Contracting Officer under paragraph (d), (f), or (k), except that if the Contractor failed to submit the termination settlement proposal within the time provided in paragraph (d) or (k), and failed

to request a time extension, there is no right of appeal. If the Contracting Officer has made a determination of the amount due under paragraph (d), (f), or (k), the Government shall pay the Contractor (1) the amount determined by the Contracting Officer if there is no right of appeal or if no timely appeal has been taken, or (2) the amount finally determined on an appeal.

(j) In arriving at the amount due the Contractor under this clause, there shall be deducted

(1) All unliquidated advance or other payments to the Contractor under the terminated portion of this contract;

(2) Any claim which the Government has against the Contractor under this contract; and

(3) The agreed price for, or the proceeds of sale of, materials, supplies, or other things acquired by the Contractor or sold under the provisions of this clause and not recovered by or credited to the Government.

(k) If the termination is partial, the Contractor may file a proposal with the Contracting Officer for an equitable adjustment of the price(s) of the continued portion of the contract. The Contracting Officer shall make any equitable adjustment agreed upon. Any proposal by the Contractor for an equitable adjustment under this clause shall be requested within 90 days from the effective date of termination

unless extended in writing by the Contracting Officer.

(l)(1) The Government may, under the terms and conditions it prescribes, make partial payments and payments against costs incurred by the Contractor for the terminated portion of the contract, if the Contracting Officer believes the total of these payments will not exceed the amount to which the Contractor will be entitled.

(2) If the total payments exceed the amount finally determined to be due, the Contractor shall repay the excess to the Government upon demand, together with interest computed at the rate established by the Secretary of the Treasury under 50 U.S.C. App. 1215(b)(2). Interest shall be computed for the period from the date the excess payment is received by the Contractor to the date the excess is repaid. Interest shall not be charged on any excess payment due to a reduction in the Contractor's termination settlement proposal because of retention or other disposition of termination inventory until 10 days after the date of the retention or disposition, or a later date determined by the Contracting Officer because of the circumstances.

(m) Unless otherwise provided in this contract or by statute, the Contractor shall maintain all records and documents relating to the terminated portion of this contract for 3 years after final settlement. This includes all books and other evidence bearing on the

Contractor's costs and expenses under this contract. The Contractor shall make these records and documents available to the Government, at the Contractor's office, at all reasonable times, without any direct charge. If approved by the Contracting Officer, photographs, microphotographs, or other authentic reproductions may be maintained instead of original records and documents.

(End of clause)
(R 1-8.701)
(R 7-103.21(b) 1974 OCT)

Alternate I (APR 1984). If the contract is for construction, substitute the following paragraph (f) for paragraph (f) of the basic clause:

(f) If the Contractor and Contracting Officer fail to agree on the whole amount to be paid the Contractor because of the termination of work, the Contracting Officer shall pay the Contractor the amounts determined as follows, but without duplication of any amounts agreed upon under paragraph (e) above:

(1) For contract work performed before the effective date of termination, the total (without duplication of any items) of

(i) The cost of this work;

(ii) The cost of settling and paying termination settlement proposals under terminated subcontracts that are properly chargeable to

the terminated portion of the contract if not included in subdivision (i) above; and

(iii) A sum, as profit on (i) above, determined by the Contracting Officer under 49.202 of the Federal Acquisition Regulation, in effect on the date of this contract, to be fair and reasonable; however, if it appears that the Contractor would have sustained a loss on the entire contract had it been completed, the Contracting Officer shall allow no profit under this subdivision (iii) and shall reduce the settlement to reflect the indicated rate of loss.

(2) The reasonable costs of settlement of the work terminated, including—

(i) Accounting, legal, clerical, and other expenses reasonably necessary for the preparation of termination settlement proposals and supporting data;

(ii) The termination and settlement of subcontracts (excluding the amounts of such settlements); and

(iii) Storage, transportation, and other costs incurred, reasonably necessary for the preservation, protection, or disposition of the termination inventory.

(R 1-8.703)
(R 7-602.29(a) 1974 APR)

Alternate II (APR 1984). If the contract is with an agency of the U.S. Government or with State, local, or foreign governments or their agencies, and if the Contracting Officer determines that the requirement to pay interest on excess partial payments is inappropriate, delete subparagraph (a)(2) of the basic clause.

(R 8-701(c))

Alternate III (APR 1984). If the contract is for construction and with an agency of the U.S. Government or with State, local, or foreign governments or their agencies, substitute the following paragraph (f) for paragraph (f) of the basic clause. Subparagraph (l)(2) may be deleted from the basic clause if the Contracting Officer determines that the requirement to pay interest on excess partial payments is inappropriate.

(f) If the Contractor and Contracting Officer fail to agree on the whole amount to be paid the Contractor because of the termination of work, the Contracting Officer shall pay the Contractor the amounts determined as follows, but without duplication of any amounts agreed upon under paragraph (e) above:

(1) For contract work performed before the effective date of termination, the total (without duplication of any items) of

(i) The cost of this work;

(ii) The cost of settling and paying termination settlement proposals under terminated subcontracts that are properly chargeable to the terminated portion of the contract if not included in subdivision (i) above; and

(iii) A sum, as profit on (i) above, determined by the Contracting Officer under 49.202 of the Federal Acquisition Regulation, in effect on the date of this contract, to be fair and reasonable; however, if it appears that the Contractor would have sustained a loss on the entire contract had it been completed, the Contracting Officer shall allow no profit under this subdivision (iii) and shall reduce the settlement to reflect the indicated rate of loss.

(2) The reasonable costs of settlement of the work terminated, including—

(i) Accounting, legal, clerical, and other expenses reasonably necessary for the preparation of termination settlement proposals and supporting data;

(ii) The termination and settlement of subcontracts (excluding the amounts of such settlements); and

(iii) Storage, transportation, and other costs incurred, reasonably necessary for the

preservation, protection, or disposition of the termination inventory.

(R 1-8.703)
(R 7-602.29(a) 1974 APR)
(R 8-701(c))

Authority: 40 U.S.C. 486(c); Chapter 137, 10 U.S.C.; and 42 U.S.C. 2453(c).

TITLE 48--Federal Acquisition Regulations System
Chapter 1
Subchapter H--Clauses and Forms
Part 52--Solicitation Provisions and Contract Clauses
Subpart 52.2--Texts of Provisions and Clauses
§ 52.219

§ 52.249-8 Default (Fixed-Price Supply and Service).

As prescribed in 49.504(a)(1), insert the following clause in solicitations and contracts when a fixed-price contract is contemplated and the contract amount is expected to exceed the small purchase limitation. The clause may also be used when the contract amount is not expected to exceed the small purchase limitation, if appropriate (e.g., if the acquisition involves items with a history of unsatisfactory quality).

DEFAULT (FIXED-PRICE SUPPLY AND SERVICE) (APR 1984)

(a)(1) The Government may, subject to paragraphs (c) and (d) below, by written notice of default to the Contractor, terminate this contract in whole or in part if the Contractor fails to--

(i) Deliver the supplies or to perform the services within the time specified in this contract or any extension;

(ii) Make progress, so as to endanger

performance of this contract (but see subparagraph (a)(2) below); or

(iii) Perform any of the other provisions of this contract (but see subparagraph (a)(2) below).

(2) The Government's right to terminate this contract under subdivisions (1)(ii) and (1)(iii) above, may be exercised if the Contractor does not cure such failure within 10 days (or more if authorized in writing by the Contracting Officer) after receipt of the notice from the Contracting Officer specifying the failure.

(b) If the Government terminates this contract in whole or in part, it may acquire, under the terms and in the manner the Contracting Officer considers appropriate, supplies or services similar to those terminated, and the Contractor will be liable to the Government for any excess costs for those supplies or services. However, the Contractor shall continue the work not terminated.

(c) Except for defaults of subcontractors at any tier, the Contractor shall not be liable for any excess costs if the failure to perform the contract arises from causes beyond the control and without the fault or negligence of the Contractor. Examples of such causes include (1) acts of God or of the public enemy, (2) acts of the Government in either its sovereign or contractual capacity, (3) fires, (4) floods, (5) epidemics, (6) quarantine restrictions (7) strikes, (8) freight embargoes, and (9) unusually severe weather.

In each instance the failure to perform must be beyond the control and without the fault or negligence of the Contractor.

(d) If the failure to perform is caused by the default of a subcontractor at any tier, and if the cause of the default is beyond the control of both the Contractor and subcontractor, and without the fault or negligence of either, the Contractor shall not be liable for any excess costs for failure to perform, unless the subcontracted supplies or services were obtainable from other sources in sufficient time for the Contractor to meet the required delivery schedule.

(e) If this contract is terminated for default, the Government may require the Contractor to transfer title and deliver to the Government, as directed by the Contracting Officer, any (1) completed supplies, and (2) partially completed supplies and materials, parts, tools, dies, jigs, fixtures, plans, drawings, information, and contract rights (collectively referred to as "manufacturing materials" in this clause) that the Contractor has specifically produced or acquired for the terminated portion of this contract. Upon direction of the Contracting Officer, the Contractor shall also protect and preserve property in its possession in which the Government has an interest.

(f) The Government shall pay contract price for completed supplies delivered and accepted. The Contractor and Contracting Officer shall agree on the amount of payment for manufacturing materials

delivered and accepted and for the protection and preservation of the property. Failure to agree will be a dispute under the Disputes clause. The Government may withhold from these amounts any sum the Contracting Officer determines to be necessary to protect the Government against loss because of outstanding liens or claims of former lien holders.

(g) If, after termination, it is determined that the Contractor was not in default, or that the default was excusable, the rights and obligations of the parties shall be the same as if the termination had been issued for the convenience of the Government.

(h) The rights and remedies of the Government in this clause are in addition to any other rights and remedies provided by law or under this contract.

(End of clause)
(R 1-8.707)
(R 7-103.11 1959 AUG)

Alternate I (APR 1984). If the contract is for transportation or transportation-related services, delete paragraph (f) of the basic clause, redesignate the remaining paragraphs accordingly, and substitute the following paragraphs (a) and (e) for paragraphs (a) and (e) of the basic clause:

(a) (1) The Government may, subject to paragraphs (c) and (d) below, by written notice of default to the

Contractor, terminate this contract in whole or in part if the Contractor fails to

(i) Pick up the commodities or to perform the services, including delivery services, within the time specified in this contract or any extension;

(ii) Make progress, so as to endanger performance of this contract (but see subparagraph (a)(2) below); or

(iii) Perform any of the other provisions of this contract (but see subparagraph (a)(2) below).

(2) The Government's right to terminate this contract under subdivisions (1)(ii) and (1)(iii) above, may be exercised if the Contractor does not cure such failure within 10 days (or more if authorized in writing by the Contracting Officer) after receipt of the notice from the Contracting Officer specifying the failure.

(c) If this contract is terminated while the Contractor has possession of Government goods, the Contractor shall, upon direction of the Contracting Officer, protect and preserve the goods until surrendered to the Government or its agent. The Contractor and Contracting Officer shall agree on payment for the preservation and protection of goods. Failure to agree on an amount will be a dispute under the Disputes clause.

(R 1-7.703-8)

Authority: 40 U.S.C. 486(c); Chapter 137, 10 U.S.C.; and 42 U.S.C. 2453(c).

48 CFR s 52.249-8

TITLE 48--Federal Acquisition Regulations System
Chapter 1
Subchapter H--Clauses and Forms
Part 52--Solicitation Provisions and Contract Clauses
Subpart 52.2--Texts of Provisions and Clauses
§ 52.219

§ 52.249-9 Default (Fixed-Price Research and Development).

As prescribed in 49.504(b), insert the following clause in solicitations and contracts for research and development when a fixed-price contract is contemplated and the contract amount is expected to exceed the small purchase limitation, except those with educational or nonprofit institutions on a no-profit basis. This clause may also be used when the contract amount is not expected to exceed the small purchase limitation, if appropriate (e.g., if the contracting officer believes that key personnel essential to the work may be diverted to other programs).

DEFAULT (FIXED-PRICE RESEARCH AND DEVELOPMENT) (APR 1984)

(a)(1) The Government may, subject to paragraphs (c) and (d) below, by written Notice of Default to the Contractor, terminate this contract in whole or in part if the Contractor fails to--

(i) Perform the work under the contract within the time specified in this contract or any extension;
(ii) Prosecute the work so as to endanger performance of this contract (but see subparagraph (a)(2) below); or
(iii) Perform any of the other provisions of this contract (but see subparagraph (a)(2) below).

(2) The Government's right to terminate this contract under subdivisions (1)(ii) and (1)(iii) of this paragraph may be exercised if the Contractor does not cure such failure within 10 days (or more, if authorized in writing by the Contracting Officer) after receipt of the notice from the Contracting Officer specifying the failure.

(b) If the Government terminates this contract in whole or in part, it may acquire, under the terms and in the manner the Contracting Officer considers appropriate, work similar to the work terminated, and the Contractor will be liable to the Government for any excess costs for the similar work. However, the Contractor shall continue the work not terminated.

(c) Except for defaults of subcontractors at any tier, the Contractor shall not be liable for any excess costs if the failure to perform the contract arises from causes beyond the control and without the fault or negligence of the Contractor. Examples of such causes include (1) acts of God or of the public enemy, (2) acts of the Government in either its sovereign or

contractual capacity, (3) fires, (4) floods, (5) epidemics, (6) quarantine restrictions, (7) strikes, (8) freight embargoes, and (9) unusually severe weather. In each instance the failure to perform must be beyond the control and without the fault or negligence of the Contractor.

(d) If the failure to perform is caused by the default of a subcontractor at any tier, and if the cause of the default is beyond the control of both the Contractor and subcontractor, and without the fault or negligence of either, the Contractor shall not be liable for any excess costs for failure to perform, unless the subcontracted supplies or services were obtainable from other sources in sufficient time for the Contractor to meet the required delivery schedule or other performance requirements.

(e) If this contract is terminated for default, the Government may require the Contractor to transfer title and deliver to the Government, as directed by the Contracting Officer, any (1) completed or partially completed work not previously delivered to, and accepted by, the Government and (2) other property, including contract rights, specifically produced or acquired for the terminated portion of this contract. Upon direction of the Contracting Officer, the Contractor shall also protect and preserve property in its possession in which the Government has an interest.

(f) The Government shall pay the contract price, if separately stated, for completed work it has accepted

and the amount agreed upon by the Contractor and the Contracting Officer for (1) completed work for which no separate price is stated, (2) partially completed work, (3) other property described above that it accepts, and (4) the protection and preservation of the property. Failure to agree will be a dispute under the Disputes clause. The Government may withhold from these amounts any sum the Contracting Officer determines to be necessary to protect the Government against loss from outstanding liens or claims of former lien holders.

(g) If, after termination, it is determined that the Contractor was not in default, or that the default was excusable, the rights and obligations of the parties shall be the same as if the termination had been issued for the convenience of the Government.

(h) The rights and remedies of the Government in this clause are in addition to any other rights and remedies provided by law or under this contract.

(End of clause)
(R 1-8.710)
(R 7-302.9(a) 1969 AUG)

UNCLASSIFIED

A-12 PROGRAM

REVIEW WITH DISCUSSION
WITH

John A. Betti
Under Secretary of Defense-Acquisition

H. Lawrence Garrett
Secretary of Navy

13 June 1990

S.C. Pace
Chairman and CEO
General Dynamics Corp.

J.F. McDonnell
Chairman and CEO
McDonnell Douglas Corp.

- - - - -

Topics for Discussion(U)

Where Are We?
- Technical Status
- Schedule Status
- Cost Status

How Did We Get There?
- What We Said in March
- Why Did We Say it?
- What Has Happened Since March?
- Are We in Control?

What Are the Major Issues?

- - - - -

Where Are We?(ω)

- Technical Status
- Schedule Status
- Cost Status

- - - - -

Where Are We – Technical Status(ω)

Weight Growth Continues as Top Concern
- But Appears to Be Under Control

No Major "Showstopper" Technical Issues

A Number of Development Items Need Watching
- Solutions in Work
- But Schedule Critical

On Balance – System Performance Is Good
- Most Items Meet or Exceed Spec
- Mission Performance Exceeds Spec
- A Few Carrier Suitability and Operational Items Do Not Meet Spec

} Excellent Overall Operational Capability

- - - - -

Where Are We – Schedule Status(ω)

Currently –

- 96+% of Drawings Have Been Released
- Over 64% of Tooling Required for First Flight Has Been Completed

But

First Flight Projected for July – Sept
Remainder of FSD Will Extend 12-14 Months Beyond Original Plan
Production Lots 1 and 2 Have Corresponding Delivery Schedule Impact
Meeting DAB Milestone IIIA Criteria Will Impact Initiation of Lot 3

- - - - -

Where Are We – Cost Status(ω)

FSD

Cost-at-Completion Analysis Still in Work

-Special Joint Corporate Red Team	Only
-MCAIR/Ft. Worth Div. Estimates	Partially Reconciled

Initial Results Indicate a Large Variance Between Estimates at Completion of FSD:

- Confidence Factor in Estimate
- Restructured Program Approach

} Potential for a Significant Increase in EAC

Production

Initial Results Indicate a Cost in Excess of Combined NTE for Lots 1, 2, 3, and 4

} Dependent Upon:
- MFG Cost
- Restructured Program Approach
- Business Base
- Total Buy

- - - - -

How Did We Get There?(ω)

What We Said in March
Why Did We Say It?
What Has Happened Since March?
Are We In Control?

- - - - -

What We Said in March(ω)

80% - Delivery of Major Components to Tulsa in August

Less Than 50% - Fly in December
- Some Parts 8-12 Weeks Beyond Need Date

- 7 Day, 3 Shift Operations
- 112 Day Span Time at Tulsa
- GVT/Proof Load on A/C #2

Going to Ceiling on FSD

- - - - -

Why Did We Say it?(ω)

Engineering 90% Released-Aircraft 1
- F-15/16/18 All Flew 10-10 ½ Months After 90% Release

CSCS Engineering Trend Showed 4-5 Months Behind June Flight Date

CSCS Tooling Trend Showed 9 Months Behind June Flight Date But Improving

Last CEO Program Review In Mid January
- Fly Sept-Dec Time Period
- Most Probable Cost slightly below Ceiling
- Possibility of Slightly Exceeding Ceiling

- - - - -

What Has Happened Since March(ω)

Impact of Revised Engineering for Weight Control
- Increased Complexity of Major Structural Parts and Tooling
- Increased Span Time for Structural Assemblies

Product Centers Could Not Absorb Sudden Ramp Up of Workload
- Forced Added Subcontracting
- Required Conversion From 3D to 2D (Security)

Experiencing 2 or 3 Attempts to Build Some Critical Path Parts

} Recent Experience Over Last 3 Months

Increased Tulsa Span Time
- Ground Vibration Test on First Aircraft
- Added One Month for Contingencies

Are We In Control?(ω)

Yes, Because
- The Design Is 96+% Complete
- We Have Frozen A/C Number 1 – Configuration
- The Tooling Design/Fab Is Under Control
- We Know where Detail Parts Are
- Recent Experience Factored Into Span Times
- Contingencies Included in Current Schedule
- Schedule Consistent With Independent Review Team

- First Time Quality on Most Complex Composite Parts
- Parts Fitting Well in the Assembly Jigs

- - - - -

Are We In Control? (Cont'd)

However the FSD Tasks Remaining Constitute a Significant Challenge

Design and Tooling for Producibility While Containing Weight Growth

Tooling, Manufacturing Processes, Quality Control and Cost of Very Large, Advanced Composite Structural Components

Completion of Development of Engine, Avionics and Subsystems

Successful Completion of Ground and Flight Tests for Production Decision Criteria

} There is Still
- A Modest Uncertainty in First Flight Date
- Some Uncertainty in the Duration of the Flight Test Program and Operational Evaluation
- Considerable Swing in Cost to Complete

- - - - -

What Are the Major Issues?(u)

- - - - -

What Are the Major Issues?(u)

1. How Best to Reschedule FSD Program
2. How Best to Rephase Production Lots 1,2,3 and 4

- Realistic Availability
  - Development Assets
  - Milestone III A and DAB Decision Criteria
- Reduction in Concurrency

3. FSD Cost Increase
4. Potential for Additional Program Elements and Cost

- Impact on USN, DoD and Congress
- Impact to Industry
- Potential to Accommodate with Restructured Program?

5. Design-to-Cost Unit Price Impact

- Determine Impact Due to Three Factors
  - --Increase MFG Cost
  - --Business Base Impact
  - --Reduction in Total Buy

6. Program and Contract Changes

- To Implement and Accommodate Above

- - - - -

Conclusions(u)

System Performance Is Good With Excellent Overall Operational Capability

The Predicted Cost of the FSD Program Will Exceed the Ceiling by a Magnitude That the Companies Cannot Absorb

The Production Lot Option Not to Exceed Prices Are Also Predicted to Exceed Those Specified in the Contract

Current Schedule Does Not Match Contract Schedule

Production Lot III Would Be Exercised Prior to Sufficient Testing to Demonstrate System Performance

The Concurrency of the Program Will Likely Lead to Milestone IIIB Not Being Met

- - - - -

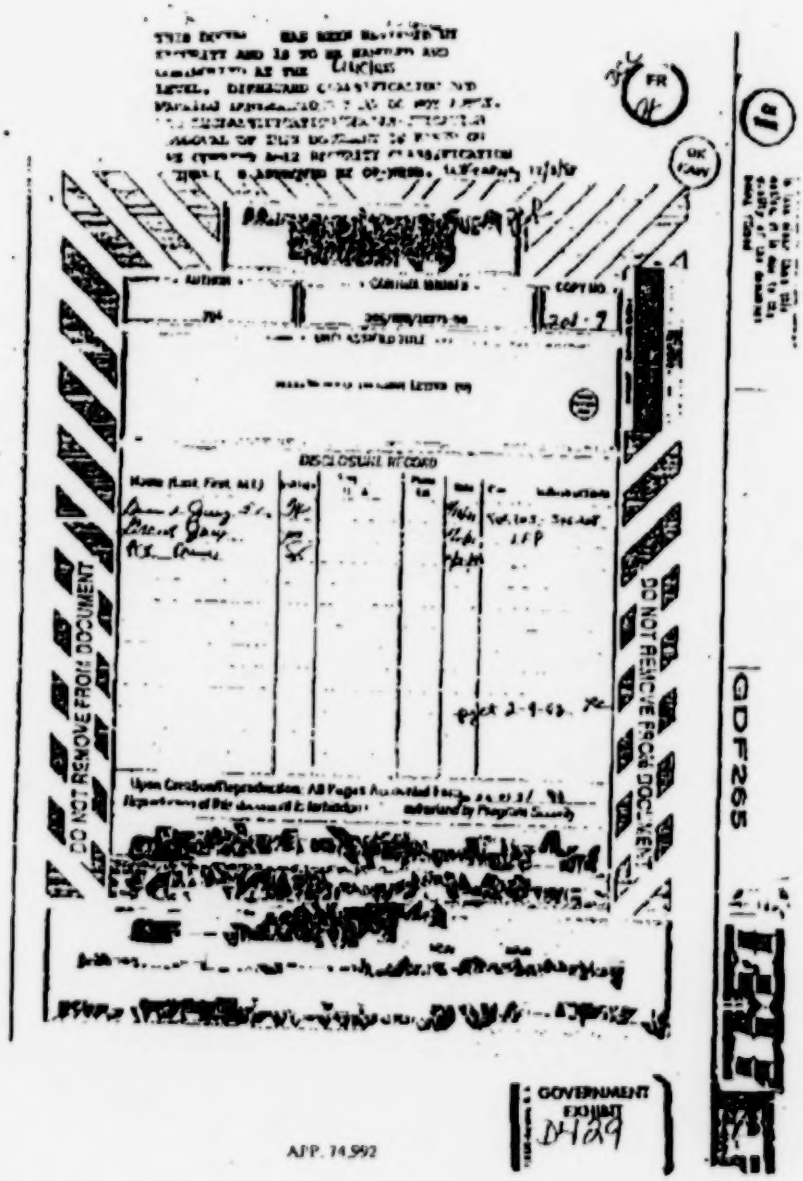
Recommendations(u)

The Program Teams, Government and Industry, Have Been Studying Various Approaches to a Restructured Program

We Should be Authorized to Complete This Study and Propose a Program and Business Arrangement

That Is In the Best Interest of the A-12 Program, Including:

- Deliveries Per Rephased Schedule for FSD and Lots 1, 2, 3 & 4
- Adjusted Specification
- Navy Added Requirements
- Contractor Claims



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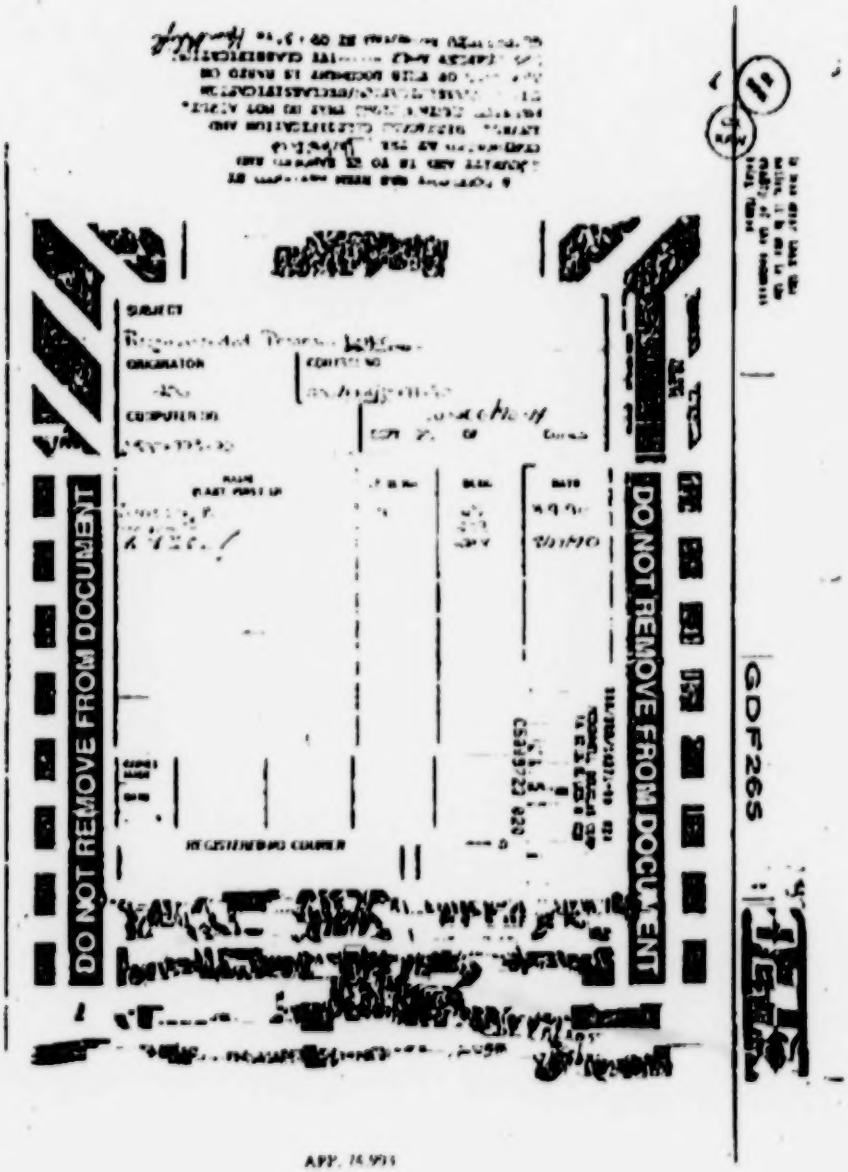
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MCDONNELL
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DIVISION
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HES-007F-100
27 June 1990

The Honorable H. Lawrence Garrett, III
Secretary of the Navy
Department of the Navy
Room 4E686
The Pentagon
Washington, D.C. 20350-1000

Dear Secretary Garrett:

(U) In response to your letter of 20 June 1990, and as discussed during our meeting on 13 June 1990, the A-12 contractual schedule is not achievable and needs to be changed. Also, it is highly desirable to modify the aircraft performance specification to reflect what is acceptable to the U.S. Navy and what is practical to achieve based upon current technical knowledge. Further, we believe that the cost at completion of the FSD contract could substantially exceed its ceiling price in a magnitude that would be very serious and unacceptable to the industry team.

(U) One of the fundamental causes for the present and just described situation on the A-12 program is

the use of a fixed price type of contract for the FSD effort, coupled with the establishment, before the aircraft was designed, of fixed price production options (or NTE's). In addition, there is invariably a drive to manage such a program as a cost type contract, requiring additional work and oversight. These problems are exacerbated in secure programs by difficulties in communicating needed and vital information from all sources. In our view, it was a mistake for the U.S. Navy to stipulate this type of contract and it was a mistake for the contractors to accept it. Both are at fault.

(U) The experience of both DOD and industry over the last 30 years has demonstrated that a success oriented schedule with new technologies involved cannot be accomplished under a fixed price type contract without the financial, schedule and specification problems which have been encountered in this program. This truth, once again, has become self evident -- this time on the A-12 program.

(U) Unfortunately, there is a further complication of the present situation. Due to the perceived reduced Soviet threat, the manufacturing business base for all defense programs, including the A-12, has become highly uncertain as to whether, when, how many, and at what rate. This clearly impacts the priced options (NTE's) for the A-12 production lots.

(U) Despite the above, our two companies have designed an aircraft which will do an outstanding job for the U.S. Navy. It is not only significantly superior to the aircraft it will replace, but also we

believe it will meet the operating requirements for which it is wanted. We accept Secretary Cheney's statement that the A-12 is a program of the highest priority. We, therefore, are recommending a rephasing of the program (schedule, budget, and contract) in the interest of achieving for the U.S. Navy the best A-12 aircraft and program in all respects.

(U) In your letter of 20 June 1990, you asked about the three schedule options we presented in our 13 June meeting. We have detailed these three in our attachments to this letter and have added a fourth, which we recommend. In constructing these program options, we have weighed the often-competing demands of technical capability, scheduled Initial Operational Capability, total budget obligation, and near-term funding profiles. We believe that our recommendation provides the best balance of these considerations by lowering Full Scale Development (FSD) and Initial Production risks while reducing total funding obligation in the FY 91-95 time period. This more conservative FSD approach will benefit out-year production costs and aircraft performance.

(U) We have reviewed the performance specification status with the U.S. Navy during the final phase of the CDR. We propose developing a top level specification that is based on the Operational Requirement (OR). Quantitative top level parameters, such as take-off wind-over-deck, strike range, weapons' accuracy and reliability, will be the basis of the A-12 specification. These will define the

required aircraft characteristics, but they will not dictate design solutions. Then all design parameters can be effectively managed to satisfy the required A-12 performance. At the conclusion of the FSD test program, the specification would be changed to reflect the demonstrated performance which would be required on production contracts.

With regard to the business arrangement, we recommend that the FSD contract with a ceiling of $4.8B be combined with the Lot I NTE price of $1.2B, thereby creating a combined ceiling price of $6.0B. Production option Lot II then would be repriced and added to the FSD and Lot I contract with a combined ceiling price. Production option Lots III and IV would be similarly priced when authorized, after the test program demonstrates confidence in the design to be produced, and then similarly added to the contract. Additional work scope supporting FSD and Lots I-IV aircraft would be added to the aggregated contract, with appropriate negotiated target cost, price and ceiling adjustments. The contractors would cost share over ceiling costs for this aggregated contract to a negotiated cap, beyond which the government would assume total liability. In consideration for these contract changes, the contractors would forego claims for which the bases have occurred prior to this date.

(U) It is recognized that the above concept for rephasing of the schedule, specification, and the business arrangement is somewhat general. We hope that it is sufficiently clear that you can give it serious consideration. After you review we would

like to be informed as to how you wish to proceed. Naturally, we are prepared to provide a detailed and fully substantiated formal proposal, based upon your direction.

Sincerely,

MCDONNELL DOUGLAS CORPORATION

/s/
John F. McDonnell
Chairman and Chief Executive Officer

GENERAL DYNAMICS CORPORATION

/s/
Stanley C. Pace
Chairman and Chief Executive Officer

[H.A.S.C. No. 101-84]

THE NAVY'S A-12 AIRCRAFT PROGRAM

JOINT HEARING

BEFORE THE

PROCUREMENT AND MILITARY NUCLEAR SYSTEMS SUBCOMMITTEE

AND THE

RESEARCH AND DEVELOPMENT SUBCOMMITTEE

AND THE

INVESTIGATIONS SUBCOMMITTEE

OF THE

COMMITTEE ON ARMED SERVICES
HOUSE OF REPRESENTATIVES

ONE HUNDRED FIRST CONGRESS
SECOND SESSION

HEARING HELD
DECEMBER 10, 1990

Mr. SKELTON. Thank you.

Mr. SISISKY. Do you know whether or not the contractors are having their own investigation of this, senior management, of how this—

Mr. GARRETT. I don't know specifically. I know that Under Secretary Betti has asked them to go and review the same things that we have reviewed.

Mr. SISISKY. One last question which I think is very important. It is my understanding, and I don't know if this is correct or not, that the original A-12 was designed to have a minimum of change once various contracts were awarded.

Were the cost overruns a result of contractor problems in meeting the original design specifications or did the contractors have problems with subsequent Navy changes in the base line contract?

Mr. GARRETT. I believe they had problems meeting the original specifications. They were difficult specifications to meet. We know how to build metal airplanes, but not quite how to build composite aircraft as well as we do metal airplanes. This is a difficult airplane to build.

We did not change our requirements in the Navy. I would know if they had. because we have a system within the Department of Navy, a program management proposal or program change proposal, that if, in fact, one is proposed, it comes to the Secretary of the Navy for approval. That is how we try to stop what used to be called "gold-plating".

Mr. SISISKY. In the original bid, how much difference was the bid between the loser there were three of them in that bid—was it a large amount or a small amount?

Mr. GARRETT. I would have to take that question for the record. It has been some time, and I don't remember what the spread was. It was not insignificant in my view.

[The following information was received for the record:]

Two offers were received in response to the Request for Proposal: one from Northrop Corporation together with Grumman Aircraft Corporation (GAC) and LTV Corporation and one from the team of General Dynamics-Ft. Worth Division and McDonnell Aircraft Company. The winning proposal was chosen upon the basis of best value to the Government. Four evaluation criteria were utilized. Cost/price was the most important factor, followed by technical, logistics and management in descending order of importance. Cost/price was evaluated based upon assessment of the contractors proposed ceiling prices for FSED and proposed Not-To-Exceed (NTE) prices for the first three production lot options; total Acquisition Cost and total Operation and Support Costs were evaluated based upon Navy estimates derived from contractor submitted data. The prices evaluated are shown in the table below.

[In billions of dollars]

Cost/Price	GD/MCAIR	Northrop/ GAC/LTV
Proposed Contract Price (TY $):		
FSED Ceiling	$4.78	$5.92
FSED Ceiling and NTE Options	$9.05	[1] $16.77
Acquisition Costs (fiscal year 1985 $)	42.90	51.50
Operating and Supporting Costs (fiscal year 1985 $)	18.70	59.50

[1] For comparison purposes and based on Lot I and Lot II proposed values, the Navy prepared a budgetary value of $3.67 billion for Lot II since Northrop/GAC/LTV did not propose a Lot III NTE.

The Northrop/GAC/LTV FSED proposed ceiling price was not in fact a ceiling. It proposed a cap of $400 million above that "ceiling", as the limit of its liability under the contract; any costs incurred in excess of that cap would be borne by the Government.

The team of General Dynamics/McDonnell Aircraft Company was rated superior to Northrop/GAC/LTV in the remaining evaluation factors including technical approach. logistics and management.

The CHAIRMAN. John Kasich and then Andy Ireland.

Mr. KASICH. Andy has done a lot of work on this. Go ahead.

Mr. IRELAND. Thank you for yielding.

Mr. Secretary, subcommittee chairman Dellums and a number of my colleagues have talked about the recommendations that you endorsed that Mr. Beach put forward. You have indicated that these recommendations acknowledged that the system was there and everything was there to make this have turned out differently.

Actually, the ball went right through the shortstop's legs. It was not a small error, it was a big error. But you have said that only fine tuning is necessary, and that there was plenty on the books, law-wise, regulation-wise, to keep this from happening.

Now, I wonder how this fine-tuning is going to help. I notice that in your testimony you say you are going to develop a "lessons learned" seminar for program executives, program managers, and key personnel. I wonder if the message there will include the fact that you can be censured and then promoted as well. I mean, we are starting off your "lessons learned" seminar somewhat on the wrong foot.

I have had calls from all over the United States from the public asking what is going on here? I don't see how you can have a "lessons learned" seminar if, with this going on, and with the censure of this gentleman and you went forward with the promotion of this gentleman to rear admiral and persuaded the Senate to support it.

How does that fit in with the message that you are going to give at that seminar?

Mr. GARRETT. I think the message is already clear.

Mr. IRELAND. That you can be promoted?

Mr. GARRETT. I considered very carefully what, if anything, I should do in response to Mr. Beach's recommendations regarding these individuals. I considered what you recommend and what you take issue with and I concluded that I would look at this record in its totality, the totality of over 20 years of naval service that led to this promotion, not just the situation that we had in hand. I concluded that, on balance, in the military to be officially censured by the Secretary of the Service Department is debilitating.

It is, I am sure, considered by many to be a slap on the wrist, as you said earlier. But it is debilitating. It is not only embarrassing to the individual, but it is probably debilitating as it relates to his future career.

It is not without significant consequence, and I took all of these issues under advisement and that was my decision for which I, of course, will be held responsible.

Mr. IRELAND. I might say in conclusion that debilitating feeling will certainly be assuaged by being promoted to rear admiral.

You say that there is some difficulty that there is an adversarial relationship that has built up here.

I guess we have a different opinion about what is adversarial.

18 December 1990

CONTRACT SENSITIVE
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MINUTES OF A-12
MEETING WITH CONTRACTORS

ATTENDEES:

GOVERNMENT

Mr. Donald J. Yockey - Acting Under Sec of Def (Acquisition)

Mr. Terrence O'Donnell - General Counsel, DOD

Mr. Dennis Trosch - Associate General Counsel, DOD

Mrs. Eleanor Spector - Dep Asst Sec of Def (Procurement)

Mr. Gerald Cann - ASN(RDEA)

Mr. Craig King - General Counsel, Navy

RADM W.R. Morris, SC, USN - Asst Commander for Contracts, NAVAIR

CONTRACTORS:

Mr. John McDonnell - CEO, McDonnell Douglas

Mr. Jerry Johnston - President, McDonnell Douglas

Mr. Bill Anders - CEO, General Dynamics

Mr. Jim Mellor - President, General Dynamics

Mr. Yockey opened meeting and invited Mr. Cann to make opening remarks.

- Mr. Cann made following points:
  - Navy needs the A12.
  - Both companies have failed cost, schedule and performance.
  - Contractors need to respond to cure notice.
  - Need to get back to SECNAV by 2 Jan, show cause to SECDEF by 4 Jan.
  - Want to proceed with FSED and Lot I.
  - Provided Navy 7.5 EAC - Means progress payments will be based on EAC.
  - Not exercise Lot II option.
  - No merit in uncertified claims.
  - Navy in tandem with OSD.
- Mr. Yockey made following points:
  - Need to provide SECDEF answer by 4 Jan.
  - SECDEF disturbed by program problems.
  - Mr. Yockey and Mr. O'Donnell charged with oversight.
  - Serious deterioration in performance of contract.
  - Participants in the room only will talk if they need to.
- Mr. John McDonnell made following points:

- Questioned depiction that it's all contactors problem. Believes U.S. Government also culpable.
- Must work out of problems together.
- Not in default. Even if they were, can't cure by 2 Jan.
- Asked "where we go from here?". Is there a way to go together?

- Mr. Yockey said that it would be helpful if claim certified.
- Mr. Anders -
  - Fixed price contracting doesn't work.
  - Can't get there if we don't change contract. If solution is for contractors alone to solve problems, they can't get there.
  - Both contractors and Government signed contract. It won't work if we don't solve together.
- Mr. Cann -
  - We have valid contract.
  - Contractors must provide response to cure notice.
  - If you want to change contract and you decide to petition under 85-804, we will consider.
  - Not inviting you to do it but you have to address issues to the government.

- Mr. Yockey - You must articulate contractor views.
- Mr. Andres - he thought main objective to get plane for the Navy
- Mr. Yockey - reaffirmed it is.
- Mr. Anders - says that Government hasn't given any indication of support for change.
- Mr. Cann reaffirmed contractors have opportunity to propose change and under 85-804 if they want to.
- Mr. Anders -
  - Says he doesn't understand why Government can't address generic solution. We jointly created a bad contract.
  - Government has a responsibility also to fix contract.
- Mr. Yockey -
  - Contractor has more information than government. Government has no superior knowledge.
- Mr. Anders -
  - Year ago Government estimated contractors 1.0 billion above ceiling. Mr. Anders said we have "mutually bad deal."
- Mr. McDonnell -
  - You are saying we have right to petition Government. What happens if they do. Seems

to him that we need to arrive at best solution - mutual agreement.

- Mr. Cann -
  - Response will depend on what contractor propose.
- Mr. McDonnell -
  - What's the best solution? How can we make best solution happen?
- Mr. Anders asked where is the bulls eye?
- Mr. Cann -
  - We will work issues with you but will not bilaterally put together 85-804.
- Mr. Yockey -
  - Fundamental concern is that we are not going to get an aircraft that we want. Will evaluate what you propose. Contractors must respond first, come in and articulate coordinated response. There's a point of no return. Get issues on table so we can deal with them.
- Mr. Anders -
  - We are not used to proposing in brittle environment that currently exists.
- Mr. McDonnell -
  - Three financial problems are loss over ceiling, termination liability and cash flow exist. Need to arrive at solution quickly.
- Mr. Cann -

- You need to propose what loss you will take. Government is not going to walk away from valid contract. There is a way under the law to deal with it - Navy has to convince OSD who has to convince SECDEF who has to convince the Congress.

- Mr. Anders -
  - Speculates unless DOD agrees its a two party problem visa-vis contract type we are unlikely to close the gap.
  - Will have to put out "warm" notices.
- Mr. Yockey -
  - There is no appetite for Government to pick up the overrun. 85-804 would be approved only in the national interest.
- Mr. Anders -
  - Cash flow problems are real. Problems have to be fixed.
- Mr. Yockey -
  - If contract converted to cost type contract the progress, payments problem is reduced.
- Mr. McDonnell -
  - You estimate the EAC at 7.5B for progress payments.
  - A 2.5B overrun!
- Mr. Anders -

- Mother nature remains a real challenge - on the edge of start-of-art. Tough to nail down future costs.

- Mr. Yockey -

  - Your chief financial officer can predict.

  Mr. Anders -

  - He can add up the numbers. The questions regard technological fog. Tough issues yet, we haven't integrated avionics. Real challenges.

- Mr. Yockey -

  - Hope you understand now is the time to fix the issues and get them behind us.

- Mr. Anders -

  - I understand the basic form of the contract can be adjusted.

- Mr. Cann -

  - Contact point for program matters is RADM Morris. Cann and King always available. Put things in writing. If you would like to float an interim package we can deal with it. Can't believe your two companies can't deal with this. It has to be economically justified. Be sure both agree with it.

- Mr. Yockey - All communications in writing.

- Mr. McDonnell & Mr. Anders - May need more conversation.

- Mr. Yockey - An interim response is possible.

- Mr. O'Donnell - Time is crucial.
- Mr. Yockey - You must know several ways to skin the cat. Be innovative. Make sure you both agree with whatever you propose.
- Meeting concluded.

DRAFT

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MINUTES OF A-12 MEETING WITH CONTRACTORS

21 DECEMBER 1990

ATTENDEES:

GOVERNMENT

Mr. Donald J. Yockey – acting Under Sec. of Def. (Acquisition)

Mr. Terrence O'Donnell – General Counsel, DOD

Mr. Dennis Trosch – Associate General Counsel, DOD

Mrs. Eleanor Spector – Dep. Asst. Sec. of Def. (Procurement)

Mr. Gerald Cann – ASN (RD&A)

Mr. Craig King – General Counsel, Navy

RADM W.R. Morris, SC, USN – Asst. Commander for Contracts, NAVAIR

CONTRACTORS:

Mr. John McDonnell – CEO, McDonnell Douglas

Mr. Bill Anders – CEO, General Dynamics

Mr. Jim Restelli – VP Contracts, McDonnell Douglas

Mr. D. Blaine Scheideman – Corporate VP Contracts, Pricing & International Offset, General Dynamics

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ANDERS: I have reflected a lot on the last meeting. Rumors abound. You can hear any you want. I hear how important the program is, how much the Navy needs it. It's reassuring if that's the position we are in, but others say we are going through a "kubucki dance" preparatory to a formal termination of the program. Is it really a fair accompli that the program is dead? Are there really two alternatives available?

CANN: It isn't dead if we can find a way to proceed and convince SECDEF that what we propose makes good sense. There are choices. This is not a charade.

YOCKEY: The requirement is there. It's a question of whether the program in its current state can satisfy the requirement. The question is: can you correct deficiencies to

provide an aircraft that meets the requirement?

ANDERS: It won't fly by 2 January. All deficiencies cannot be corrected. Can we deliver a satisfactory aircraft for the Navy? Mother nature won't allow correction of all defects. We'll do the best we can and the Navy has to decide if that's good enough. It's going to be a good airplane – one I would like to fly.

MCDONNELL: Does the $7.5b EAC include FSED and Lot I, or just FSD?

CANN: FSD alone.

YOCKEY: The real question is are you prepared to complete FSD under the FPI contract for whatever it takes.

MCDONNELL: It has got to get reformed to a cost type contract or we cannot do it. We need some form of PL 65-804.

ANDERS: We can propose solutions if we understand the problem. We are studying the vibes.

MCDONNELL: We're working the problem.

YOCKEY: Whatever you propose you need to tell us what costs you're willing to assume. Any reformation will not involve our picking up all costs from here on out.

ANDERS: We expressed the view in our last meeting that this is not all our problem. There are also certain financial limits we can accept.

YOCKEY: If you believe that you have the basis for relief under PL 85-804, we haven't seen it yet. If not an 85-804 solution, you need to tell us how you'll proceed under the contract.

MCDONNELL: We will submit a certified claim.

YOCKEY: If you propose PL 85-804 solution, you waive claims.

ANDERS: The cash flow issue is worse than the loss problem. We're selling at less than 50 percent of book value. The best fighter houses in the world are in the worst positions. We may not be able to proceed from a financial point of view. Your people have told the press, to our dismay, we are not the healthiest financial

organizations. Our stocks are the most discounted in the defense industry.

MCDONNELL: The solution has to address near term cash.

ANDERS: The cash has to be addressed right away.

YOCKEY: The government is not going to take unlimited responsibility.

MCDONNELL: We hear your message. We have to take some pain. Are you also saying that we will have to take additional risks in future?

ANDERS: Your cost estimate indicates how hard it is to reinvent this wheel. If we had been Northrop, we would not have had this problem. Maybe our guys are using the wrong rules of thumb in projecting. If we were starting from scratch, you wouldn't offer and we would not take a fixed price contract. Our joint objective should be to get the best airplane. You must know something we don't with your $7.5B EAC.

MCDONNELL: What Bill is saying is that we learned our lesson. We should

not have taken a fixed price contract with this sort of financial risk.

YOCKEY: Whatever we work out, and if we agree, there has to be some sharing. You will need to take some pain up-front. Best case – CPIF contract if we can convert.

ANDERS: How do we try to sell to the Hill? How do we have some real incentives and work under that.

CANN: We are formulating some ideas to address this. RADM Morris can sit down with your people and discuss when you tell us what your going to do.

ANDERS: First we have to decide what we want to do. The "how" of it we can work together. We won't take another fixed price effort.

YOCKEY: You have to respond to the show case. You need to articulate what you would like to do. In doing so, make sure you're taking responsibility and some continuing responsibility. If we consider there is merit, we will entertain your proposition.

ANDERS: Would you be surprised if we expected DOD to take some risk? If we have the right size but the wrong shape, we don't want to lose the program.

YOCKEY: You'll have to justify your position to the Navy. They'll then come to me and O'Donnell.

CANN: The idea is to have the frame of reference, the boundary conditions defined.

YOCKEY: Mr. O'Donnell and I feel there is something worth pursuing here which we will have to define to SECDEF.

CANN: The Navy has to have a program that we can persuade DOD and Congress is worth pursuing and that we know how to pursue it.

ANDERS: The real issues – 85-804 is not a specification solution what you see is what you get – it's a financial resolution.

YOCKEY: The Navy is going to express concerns to you with regard to management. I am particularly concerned that we have something, an aircraft with a

potential for growth. I would like to see some representation that the aircraft will be suitable for the Navy requirement.

ANDERS: This is the state of the art. We can't guarantee in detail what the aircraft will do. We don't know the unknown unknowns. Having been burned badly on large composites, we think we are out of the woods. All we can do is bust our tails.

YOCKEY: If you're telling me that you have to rediscover the laws of physics, I am concerned.

MCDONNELL: We're fixing the problems. We are doing the large composites now.

ANDERS: We haven't flown this aircraft. This is a highly integrated aircraft. It should have been a CPAF contract from day one. Technical reputation doesn't do any good if you're in Chapter 11. We need to emphasize the cash problem. Time is a problem.

YOCKEY: You can warrant performance analytically. The technical

reputation of your companies should be on the line.

ANDERS: I want to emphasize the cash problem. Boundary conditions would be acceptable up-front.

YOCKEY: If you want to trade off near term cash for long term losses that can potentially be worked.

CANN: We need to have a better understanding of how you would organize. Review your contract. You signed a teaming agreement that you're not living up to. You don't have a collocated program office.

MCDONNELL: One of the problems was the issue of getting people physically collocated.

ANDERS: Management is a third order issue. To spend a lot of time on a management plan for a program that is going to stop is a waste of time.

YOCKEY: Whatever is worked out has to be resolved in a detailed fashion -- down to the 4th or 5th levels of detail.

MCDONNELL: We will work out the management issue.

ANDERS: The fixed price nature of the contract precluded good management. I did a study four years ago indicating we were heading down a slippery slope with fixed price contracts. We are not in the business of winning lawsuits. We would rather build airplanes. If we can work this out, we'll unleash everything on the Hill that we can to help.

YOCKEY: That cannot influence our decision.

ANDERS: I understand.

MCDONNELL: The decision shouldn't be to go for a termination because you think Congress won't go along.

YOCKEY: The basis for the letter is that you have failed to make progress. We think we have the right to terminate for default. We can pursue claims. We have other options.

ANDERS: I find this helpful.

YOCKEY: If you conceptually come in with something of merit, we will work it.

CANN: We'll get together early afternoon of the 2nd of January.

O'DONNELL: We need to make substantial progress. It needs to be tied together – financial, management, technical, legal. We appreciate you can't build the entire structure by the 2nd.

MCDONNELL: We need to deal with all of them!

O'DONNELL: You need to make substantial progress.

YOCKEY: How are you going to build a product for the Navy? You have to warrant the product without going through any substantial redesign.

ANDERS: We have an entirely new aircraft, it's not mature. It's a different breed of cat.

YOCKEY: Reinforcing your view, perhaps the EAC is higher than you are projecting.

CANN: The differences in the EAC are accounted for by the fact that we

took a more pessimistic view of your ability to turn things out right the first time.

SCHEIDEMAN: Does the $7.5B EAC include new work? The funding profile is also an issue.

MORRIS: The $7.5B EAC does not include any new work. It estimates costs based on the current contract.

CANN: You can propose what you want. We need to make decisions on the FY92 budget.

YOCKEY: We are also concerned with the unit cost. We can ill afford to redesign.

ANDERS: This aircraft has a lot of potential for what the heavy attack guys need. It has a lot going for it on paper. Until I see it going around the traffic pattern, I'll be concerned. Problems later on can eat you alive.

CANN: We will see you at 1:00 PM on the 2nd in Mr. Yockey's office.

YOCKEY: We can all be available to talk to you. Stick to the issues and

provide us your proposal in writing.

ANDERS: I think we have heard the general shape of it if not the size for the solution.

MCDONNELL DOUGLAS
MCDONNELL AIRCRAFT COMPANY
P.O. Box 516
St. Louis, MO 63166

GENERAL DYNAMICS
FORT WORTH DIVISION
P.O. Box 748
Fort Worth, TX 76101

0050-FW#0110-3325
2 January 1991

Subject: Contract N00019-88-C-0050, A-12
Advanced Tactical Aircraft Program -
Response to NAVAIR Letter 4200 AIR-02

To: Department of the Navy
Naval Air Systems Command
Washington, D.C. 20361

Attention: AIR-02/Rear Admiral W. R. Morris

Reference: (A) NAVAIR Letter 4200 AIR-02,
dated 17 December 1990,
General Dynamics Log No. A90-1213

This response is to your letter, Reference (A). While the contractors will not meet delivery schedules or certain specifications of the original contract, or the revised FSD delivery schedule unilaterally imposed by a Navy contract modification, for the reasons set forth below, the contractors are not in default of the A-12 contract.

The notice alleges that the contractors have failed to fabricate parts in time to meet the delivery schedule for FSD aircraft, and that the contractors will not deliver Lot 1 aircraft in accordance with the contract schedule. The contract delivery schedules for FSD and Lot 1 aircraft are, in our view, invalid. The status of the A-12 Program demonstrates that the fundamental factual assumptions of the original contract, with respect to schedule and achievability of certain specification requirements, were gravely

mistaken. As the Program has developed, it has become clear both to the Team and to the Navy that the schedules and certain other specification requirements, such as weight, were impossible to satisfy. In these circumstances, there is not an enforceable schedule or specifications against which to measure the Team's performance.

The Contractors have been forthright with the Navy throughout this Program in surfacing problems as they have developed. We have worked with the Navy in good faith to overcome these problems, and to deliver the best possible aircraft. The Navy cannot now ignore the fact that it has been informed of these difficulties, or that it has encouraged the Team to continue performance despite its knowledge that the delivery schedules and the literal terms of certain specification requirements were not achievable, nor can the Navy deny that the Team, in reliance on these encouragements, has diligently prosecuted the work at enormous expense to both companies.

Despite the lack of valid delivery schedules, the Team has been fully committed to the success of the Program, and has diligently prosecuted the work relating to fabrication of parts and all other aspects of performance in a manner that reasonably assures a satisfactory completion of the FSD and production phases of the A-12 Program.

First, with respect to the design and manufacturing process, the Team has made significant progress in the past several months.

Nearly all structural drawings have been released to manufacturing. Since July 1990, 2,030 tools have been completed. Manufacturing processes and yields are dramatically improved. Most of the large complex composite parts for the first aircraft are complete, and 50% of the major structural assembly for that aircraft has been completed. A major transfer of composite fabrication work from GDFW to McAir has been accomplished, improving schedule confidence.

Second, the Team has made major advances in the A-12 Test Program. Wind Tunnel tests are 92% complete, well ahead of need as measured against current schedules. Signature tests have validated the adequacy of the LO design. Structures testing, while admittedly affected by prior fabrication difficulties, is proceeding in a manner that will permit completion of a fully specification-compliant static test prior to first flight. Survivability and vulnerability testing, not even required for first flight, is 77% complete, and all tests will be complete prior to first flight.

Third, significant improvements have been made in the procurement of purchased parts from A-12 suppliers. Based on the Navy's unilateral FSD schedule, substantially all of the approximately 20,000 procured line items will be available to meet manufacturing need dates, and, as of November 30, 1990, 95% of Aircraft 1 procured requirements have already been purchased and delivered. 98% of procured material requirements for system and structural tests (fuel, ECS, electrical, etc.) have been

purchased and delivered. The remaining 2% will be available to meet established test dates.

Performance problems relating to the multifunction antenna, which the Team contends arise out of the impossible specification requirements imposed by the Navy, have been largely overcome. The new design that resulted from the intensive efforts on this antenna was enabled by the invention of a radome that represents an advance in the state-of-the-art.

The multifunction radar system, awarded to Westinghouse following Norden's termination for default in April 1989, is now ahead of need. Major radar design review milestones and initial deliveries have been successfully completed.

Concurrent with this significant progress, the Team has remained attentive to A-12 Integrated Logistic Support requirements, all of which will be available to support early aircraft as they are delivered to test sites.

The success of these activities has been enhanced by the contractors' organizational changes, including GDFW's and McAir's assignment of new Program Managers. A single management focus for A-12 Manufacturing was established when a senior McDonnell Aircraft Company executive was assigned as Vice President, A-12 Manufacturing, with executive authority and responsibility for all Manufacturing Operations at McAir, GDFW, and Tulsa.

The notice also states that the Team's alleged "failure to meet specification requirements, such as aircraft weight, jeopardizes the carrier suitability of your design." The team's design for the A-12 was found to be technically sound during the exhaustive Critical Design Review. While there is a shortfall against some parameters of the original technical specification, we believe that the current design meets the operational objectives. It exceeds the specification and operational requirement in range/payload. As described in the Team's Claims submittals, and as the Navy has itself acknowledged, the weight specification is literally impossible to achieve. The Navy, therefore, has no right to demand adherence to that requirement. Further, the Navy has known at least since mid-1988 (if not before award of the FSD contract) that the weight specification is not achievable, and therefore has no right to insist now that it be satisfied. Projections of aircraft weight at IOC have not changed in nearly a year.

The weight issue should not be permitted to detract from the revolutionary technical advances achieved by this Program, for, despite the exceptionally difficult technical challenge presented by this revolutionary design, during the Design Review Board (DRB) process that was completed in October 1990, the Team convincingly demonstrated that the A-12 design is technically satisfactory. Over 400 significant technical issues were addressed and resolved during this DRS process.

Finally, the notice demands that the schedule,

weight, and other unspecified "conditions" be "cured" by January 2, 1991. Compliance with the demand is unachievable as the Navy well knows, and is not required as a matter of law or equity.

As described in the Team's Memorandum in Support of Contract Restructure, dated November 9, 1990, contractor development and manufacturing activities have been substantially and excusably delayed and impacted by acts and omissions of the government. Very important information vital to the performance of the contract, available to the Government, was not provided. In addition, the Contract may have been void from the beginning, by reason of its award in violation of statutes and regulations requiring suitable risk reduction in development efforts prior to award of a fixed price development contract. The Navy's conduct renders invalid the delivery schedules set forth in the contract, and entitles the contractors to an equitable adjustment in both schedule and price for FSD and Lot 1. Moreover, as the contract is incrementally funded, the contractors' obligation prior to full funding is limited to performance within the available funding. For these same and other reasons, the schedule unilaterally imposed by the Navy is also not valid; and, furthermore, it is unreasonable inasmuch as it purports to schedule FSD aircraft deliveries after delivery of Lot 1 aircraft.

We provide this response to demonstrate our commitment to the Program, and specifically to address the concerns you have raised. Our greater

objective is to conclude successfully an equitable restructure of the contract and clear the way for the design and delivery to the Navy of a superior new attack aircraft that will allow the Navy to meet the challenging threats in the years ahead. We trust that the Navy's intention remains, as does ours, to complete this effort and to provide this critically important weapon system to the fleet. Therefore, we are submitting under separate cover a proposal to restructure the program on a viable basis.

MCDONNELL DOUGLAS CORPORATION
McDonnell Aircraft Company

/s/ Roger J. Witte
Roger J. Witte
Vice President
Contracts and Pricing

GENERAL DYNAMICS CORPORATION
Fort Worth Division

/s/ George Kostohryz
George Kostohryz
Vice President
Contracts

DRAFT

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MINUTES OF A-12 MEETING WITH CONTRACTORS

1000 -- 02 JANUARY 1991

ATTENDEES:

GOVERNMENT

Mr. Donald J. Yockey - Acting Under Secy of Def (Acquisition)

Mr. Terrence O'Donnell - General Counsel, DOD

Mr. Dennis Trosch - Associate General Counsel, DOD

Mrs. Eleanor Spector - Dep Asst Sec of Def (Procurement)

Mr. Gerald Cann - ASN(RD&A)

Mr. Craig King - General Counsel, Navy

RADM W.R. Morris, SC, USN - Asst Commander for Contracts, NAVAIR

Capt. Marc Pelaez, USN - Exec Asst/Naval Aide to ASN(RD&A)

CONTRACTORS

Mr. John McDonnell - CEO, McDonnell Douglas

Mr. Bill Anders - CEO, General Dynamics

Mr. Jim Restelli - VP Contracts, McDonnell Douglas

Mr. D. Blaine Scheideman - Corporate VP Contracts, Pricing & International Offset, General Dynamics

Mr. Jerry Johnston - President of MACAIR

Mr. Jim Mellor - President of General Dynamics

Mr. Robert Duesenberg - Counsel with General Dynamics

Mr. John Sant - Senior VP of MACAIR

Mr. Jim Cunnane - VP of Financial Management for General Dynamics

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ANDERS:

-- Claims certified

-- With us we have response to letter

-- Detailed description of our proposal

-- Viewgraphs which depict our proposal to equitable restructure

-- We request that you give us maximum feedback to resolve this

-- Our objective is to assume success of the A-12 program

-- Focused on FSD & Lot 1

-- Our view both government and contactors were party to the problem and must be party to solution

-- A-12 is a revolutionary design

-- pushes state of art

-- challenging but duable in team working environment

-- We have had problems with composites manufacturing but they are behind us

-- still have avionics ahead of us

McDONNELL: -- Our avionics people feel it is duable

ANDERS: -- Both companies committed --

-- prior to FSED each company put $120M of our money in the program

-- currently financing a significant portion

-- in this down-turn environment we want to be involved especially considering future production potential

-- problem though is the fixed price contract

-- this type of contract limits the Navy's ability to effectively manage

-- unreasonable financial burden and risk placed on contractors

-- key points of restructuring proposal

-- contractor team assumes $1B of overrun

-- waive our claim of $1.6B

-- implement restructure under Public Law 85-804

Provided FSD and Lot 1 restructure to:

-- cost reimbursement/fixed loss contract

-- cash flow must be resumed

McDONNELL: -- $1B fixed loss

-- $500M over FSD & Lot 1

-- Other $500M credited over first 250 a/c @ $2M per a/c

YOCKEY: -- What if we go to flight test and find big problem that program won't go -- how will the government get the other $500M?

McDONNELL: -- It does depend on production

YOCKEY: -- So the $1B is not really for FSD and Lot 1

ANDERS: -- Yes, it really is but it depends on you (gov't) to go to production

McDONNELL: -- Describes restructure recommendation

-- FSD and Lot 1 would need to be changed to a cost

reimbursement contract with a fixed loss

-- with award fee provisions

  -- outyear production would have to be negotiated

-- An important element of any deal is that we need immediate cash flow improvement

  -- currently getting none

  -- this is an essential condition

  -- We propose 100% flexible progress payments with a loss ratio

  -- We will have a new EAC by mid Jan and propose to use that for the restructuring

  -- Let me clarify, the flex payment is meant to cover the 90 day restructure period then we would go to cost plus

  -- This proposal assumes continued funding under Clause H-7 of contract which has a $553M payment due 7 Jan 91

-- Regarding PL 85-804

We are proposing that it be done under fairness, mistakes or residual powers and not

essentiality/financial requirement

-- As part of the deal we also will waive $1.6B in claims

CANN: -- Waiving claims doesn't mean they won't be resolved later

McDONNELL: -- We will withdraw these claims

YOCKEY: -- Weren't the claims McDonnell Douglas'

ANDERS: -- No -- both companies

McDONNELL: -- There are some other issues to resolve

-- Need Navy assistance in quality requirements on accepting parts for these initial airplanes

-- The DRPOs are under pressure and not applying consistent standards

YOCKEY: -- They should be following basic 9858 procedures

McDONNELL: -- Yes, but they are not being equitably applied

YOCKEY: -- There will be no backing away on quality

McDONNELL: -- This is the restructure time table as we see it:

○ USN/DOD acceptance in principle	Early January
○ Approval of progress payments	Mid January
○ Planned availability of MDC/GD EAC	Mid January
○ Definitize A-12 technical baseline	Mid-late January
○ Definitize Memorandum of Agreement	Late January
○ MDC/GD file application for Public Law 85-804 restructuring per MOA	Late January
○ DOD completion of Public Law 85-804 documentation and congressional submittal	Early February
○ Completion of Congressional notification period	Mid April
○ Implementation of restructured contract	Mid April

YOCKEY: -- When you say definitize the technical baseline you are saying the spec is what the plane is today not what is in the contract

McDONNELL: -- Yes -- as discussed in CDR (Critical Design Review)

McDONNELL: -- I would like to summarize by saying that the Fixed Price Contract limits ability to manage and must be restructured

YOCKEY: -- Both you and Navy are limited

McDONNELL: -- Basically we are willing to take $1B loss and waive $1.6B claim and deliver a/c for Navy

YOCKEY: -- This is movement in the right direction -- I ask that you leave a copy of your letter describing your position and give us 15-30 minutes to confer--there are certain issues Navy wants to consider--we need to discuss with Attwood--I will see Attwood 3:30-4:00 today and can give you an answer by 1800

GOVERNMENT ONLY SESSION

YOCKEY: -- Interesting

CANN: -- They came further than I anticipated

YOCKEY: -- Look at what they are really offering--taking $500M now but GD has already taken most of that

KING: -- Need to see this as a $2.6B package and discuss further its composition

YOCKEY: -- But you are buying the plane as is

-- There may be nothing wrong with taking some reduction in specs

-- I'm concerned with them saying take quality out--there may be something there

CANN: -- It was not clear if the loss they were going to take was FSD and Lot 1

MORRIS: -- Both

YOCKEY: -- There is the genesis of a deal here if we could jack them up another $1B

SPECTOR: -- Could structure a deal $500M up to $6.5B -- then could get some percentage say 80/20

YOCKEY: -- So get $1B up to 6.5 then up to $7.5 B could go 80/20

CANN: -- The central issue is the basis under which they want to come in under Public Law 85-804

YOCKEY: -- McDonnell Douglas discussed alternatives--we could try it their way but no guarantees

TROSCH: -- We can go forward under any premise we want

YOCKEY: -- We need to tell them how we

would go

-- We also need to tell them they are $1B off

KING: -- What if we say look at a $2.6B package but how the split is taken is crucial and we need to look at their books for 85-804 when talking this kind of money

SPECTOR: -- They can't take another $1B

O'DONNELL: -- $500M of the deal is on the 250 aircraft

CORRECTION
THE PREVIOUS DOCUMENT(S)
MAY HAVE BEEN FILMED
INCORRECTLY.....

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SPECTOR: -- They can't take another $1B

O'DONNELL: -- $500M of the deal is on the 250 aircraft

SPECTOR: -- We could escalate the $500M

YOCKEY: -- Problem is this is only a $500M offer

(To CANN): -- Do you want to see what kind of offer you can pull together with your guys?

CANN: -- You meet with Attwood at 3:30 and we will go and scrub this thing -- we will get back with the contractors at 5:30P.M.

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MINUTES OF A-12 MEETING WITH CONTRACTORS

1630 – 02 JANUARY 1991

ATTENDEES:

GOVERNMENT

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Capt Marc Pelaez, USN – Exec Asst/Naval Aide to ASN (RD&A)

CONTRACTORS

Mr. John McDonnell – CEO, McDonnell Douglas

Mr. Bill Anders – CEO, General Dynamics

Mr. Jim Restelli – VP Contracts, McDonnell Douglas

Mr. D. Blaine Scheideman – Corporate VP Contracts, Pricing & International Offset, General Dynamics

Mr. Jerry Johnston – President of MACAIR

Mr. Jim Mellor – President of General Dynamics

Mr. Jim Cunnane – VP of Financial Management of General Dynamics

Mr. John Sant – Senior VP of MACAIR

YOCKEY: -- Let's get right to it. You have a proposal on table.

-- It doesn't work – it's 50% of the way there.

-- There are a couple of options

You rethink T for D

We unilaterally direct you to perform and work claims

ANDERS: -- That's disappointing – what are you trying to accomplish?

YOCKEY: -- Our EAC is $7.5B – we are willing to take 25% you cover 75% -- beyond 7.5 we would cover 90% you 10%. We are perfectly willing to work out payment period over time. Take both FSD and Lot 1 – there is a $3B spread of overrun by our numbers. We would take approximately $1B – you take approximately $2B. Of that amount we would hope to see something like $500M now and the rest over 10 yrs but not against production aircraft.

ANDERS: -- But production is not in your control – we wouldn't carry this without assured production.

YOCKEY: -- This is repayment of a debt.

ANDERS: -- Our view is that both parties are responsible.

YOCKEY: -- You offered claims but the process is a long one and historically you might at best see 25 cents on the dollar.

ANDERS: -- What if the production program does not go ahead? Does what

you have put on table go away if production goes away?

YOCKEY: -- We are loaning you this money.

McDONNELL: -- This is a big cash program.

ANDERS: -- We're putting in $150M/month – already have $800M in this.

YOCKEY: -- Can't solve this here, you have options for corporate financing.

McDONNELL: -- No one could cover something of this magnitude.

YOCKEY: -- You get with the Navy and discuss.

ANDERS: -- I guess we didn't get the point across of joint responsibility and the inappropriateness of using a fixed price in a high risk classified program especially considering the knowledge you have.

YOCKEY: -- Bill, if that is your concern submit it as a claim and we'll look at it.

McDONNELL: -- Claims are not an alternative as long as we have a cash problem. Would you consider flex

payments while claims process proceeds?

YOCKEY: -- I guess it's possible.

McDONNELL: -- You've made your position clear – we will have to look at this to see if restructuring is possible.

YOCKEY: -- Money has value so we are picking up greater than 25% of the cost. That's the best deal we can offer.

McDONNELL: -- Are you available in the AM to talk with us?

YOCKEY: -- Yes.

O'DONNELL: -- $500M of the deal is on the 250 a/c

DRAFT

CONTRACT SENSITIVE
FOR OFFICAL USE ONLY

MINUTES OF A-12 MEETING WITH CONTRACTORS

1730 – 02 JANUARY 1991

ATTENDEES:

GOVERNMENT

Mr. Gerald Cann – ASN (RD&A)

Capt. Marc Pelaez, USN – Exec. Asst./Naval Aide to ASN(RD&A)

Mr. Craig King – General Counsel, Navy

RADM W.R. Morris, USN – Asst. Commander for Contracts, NAVAIR

CONTRACTORS:

Mr. John McDonnell – CEO, McDonnell Douglas

Mr. Bill Anders – CEO, General Dynamics

Mr. Jim Restelli – VP Contracts, McDonnell Douglas

Mr. D. Blaine Scheideman – Corporate VP Contracts, Pricing & International Offset, General Dynamics

Mr. Jerry Johnston – President of MACAIR

Mr. Jim Mellor – President of General Dynamics

Mr. Jim Cunnans – VP of Financial Management of General Dynamics

Mr. John Sant – Senior VP of MACAIR

CANN: -- It's clear to us that we need to get back to Cheney and Attwood by Friday. It's clear the problem is we may have to present 2 positions to Cheney if you take Yockey's statement on fact and believe an EAC of $6.5. Let met tell you how we looked at it. We knew about the $2B bogey but were looking at a 40/60 split. We became aware of the 80/20 option without payback over 250 production aircraft about 30 minutes before the meeting. OK, let's see if we can get to a resolution.

ANDERS: -- How about 85-804 being out – we all thought that...

CANN: -- No! 85-804 is definitely on the table. One thing you need

to understand about 85-804 is we will only do it with a financial audit and under the position of essentiality.

McDONNELL: -- OK, if it is the program.

KING: -- It will go to the Corporation.

ANDERS: -- How about the view that DOD screwed up?

CANN: -- Some precedent issue – if we were to follow that approach we would open up all contracts.

ANDERS: -- For DOD to take position they can't right a wrong isn't right.

McDONNELL: -- Well, let's look at the essentiality concept -- an audit determines how much the burden is – then it is open ended.

CANN: -- No one will let us go forward without an audit.

McDONNELL: -- Yes, but how will audit be used. The very act of the auditors going out to discuss with bankers will result in it becoming a self-fulfilling

prophecy.

ANDERS: -- How can Attwood take this position?

CANN: -- Most of this should have surfaced earlier.

ANDERS: -- But if you don't know you had a problem--how can you surface it? Also the government was very familiar with the B-2 and knew a lot more than was shared with us.

McDONNELL: -- There's a big concern about what we don't know. Whole thing is like a snowball.

CANN: -- Setting that aside we can only go forward with 85-804 based on essentiality. Further, Yockey based his discussions on a $7.5B EAC.

ANDERS: -- The issue is risk--we can't get there from here--you could drive this whole thing out of sight.

ANDERS: -- We would have to write this off now--if it's not contingent you have to write it off.

McDONNELL (to ANDERS): -- If you can make it contingent would that be OK?

ANDERS: -- Yes.

CANN: -- What we need tomorrow is another meeting with Yockey to lay out finance 101. You will need to address the $2B and how you pay it back. We need to get to a cost plus environment.

ANDERS: -- We are concerned about the risk we will assume if we get the aircraft in test and don't meet the spec.

CANN: -- We are not hung up on the spec issue the way it was portrayed today.

ANDERS: -- There are 2 levels of specs!

Macro specs.

Micro specs.

The DRPOs are going crazy-- they are afraid to pass anything.

CANN: -- We can work that issue.

ANDERS: -- Let's say we can get the thing split, part of it contingent,

then the size of the nut is too big. We can't absorb it.

CANN: -- Well what we need are the following:

- o agree with us on your best position
- o decide to pursue program or not
- o you need to lay out the economics 101 for tomorrow.

DRAFT

CONTRACT SENSITIVE
FOR OFFICAL USE ONLY

MINUTES OF A-12 MEETING WITH CONTRACTORS

(NAVY ONLY)

0800 – 03 JANUARY 1991

ATTENDEES:

GOVERNMENT

Mr. Gerald Cann – ASN (RD&A)

Mr. Craig King – General Counsel, Navy

RADM W.R. Morris, USN – Asst. Commander for Contracts, NAVAIR

Capt. Marc Pelaez, USN – Exec. Asst./Naval Aide to ASN(RD&A)

CONTRACTORS

Mr. John McDonnell – CEO, McDonnell Douglas

Mr. Bill Anders – CEO, General Dynamics

Mr. Jim Restelli – VP Contracts, McDonnell Douglas

Mr. D. Blaine Scheideman – Corporate VP Contracts, Pricing & International Offset, General Dynamics

Mr. Jerry Johnston – President of MACAIR

Mr. Jim Mellor – President of General Dynamics

Mr. Jim Cunnane – VP of Financial Management of General Dynamics

Mr. John Sant – Senior VP of MACAIR

ANDERS: -- Sad to report we do not have a solution to Yockey's problem. Tried to list what the givens were and we had trouble sorting it out. Having made our best offer and since Yockey's position is not workable--we would be better off with an orderly close out.

CANN: -- Then set that aside and lets look at your proposal. We need to ensure we understand how you view the solution.

ANDERS: -- A 70/30 split is not justified from equity viewpoint. If issue of contingent deferral is not acceptable then we may

as well go home.

KING: -- The contingent issue is just Yockey's.

ANDERS: -- We can package a better offer if we can go with a contingent position.

CANN: -- The only thing we need to straighten out is that based on contractors proposal (as modified) we need to make sure it is understood that we will only do 85-804 on essentiality and I have to make sure that it is acceptable.

McDONNELL: -- I'd like John Sant to address the issue of essentiality.

SANT: -- This is workable if you look at essentiality on the basis of this contract alone and what it will do in financial exposure. If we were looking at cash projections of this program and couple that with our published financial disclosures to determine essentiality, it could work.

ANDERS: -- If you do that and get a determination that the contract won't drive you over the edge--that means no relief until it actually does.

CANN: -- Look, we need the airplane and we want to get in a different management mode. A key to any restructure is that this is an essential program to the government.

ANDERS: -- You are arguing mutual mistake in part. In our view there is a necessity to admit mutual mistake. There is a limit to how much industry will pick up of the tab.

McDONNELL: -- In the past 85-804 had been limited to a part of the corporation involved in the contract. The question is can you limit it?

KING: -- We are talking as if this is a legal set of rules--it's not--it's political.

ANDERS: -- You have to get the twist from mutual mistake to essentiality.

CANN: -- We need to adjourn to meet with OSD.

DRAFT

CONTRACT SENSITIVE
FOR OFFICAL USE ONLY

MINUTES OF A-12 MEETING WITH CONTRACTORS

0900 – 03 JANUARY 1991

ATTENDEES:

GOVERNMENT

Mr. Donald J. Yockey - Acting Under Sec. of Def. (Acquisition)

Mr. Terrence O'Donnell - General Counsel, DOD

Mr. Dennis Trosch - Associate General Counsel, DOD

Ms. Eleanor Spector - Dep. Asst. Sec. of Def. (Procurement)

Mr. Gerald Cann – ASN (RD&A)

Mr. Craig King – General Counsel, Navy

RADM W.R. Morris, SC, USN – Asst. Commander for Contracts, NAVAIR

Capt. Marc Pelaez, USN – Exec. Asst./Naval Aide to ASN(RD&A)

CONTRACTORS

Mr. John McDonnell – CEO, McDonnell Douglas

Mr. Bill Anders – CEO, General Dynamics

Mr. Jim Restelli – VP Contracts, McDonnell Douglas

Mr. D. Blaine Scheideman – Corporate VP Contracts, Pricing & International Offset, General Dynamics

Mr. Jerry Johnston – President of MACAIR

Mr. Jim Mellor – President of General Dynamics

Mr. Robert Dusenberg – Counsel with General Dynamics

Mr. John Sant – Senior VP of MACAIR

Mr. Jim Cunnane – VP of Financial Management for General Dynamics

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ANDERS: -- We do not have a counter offer. We are not ready to give up but we are confused. The way we see it we made an offer we thought was responsive in form and size to what we thought we heard in conversations in the past including restructure to cost plus. Right or wrong we feel

there is a major issue of mutual culpability. Your counter offer was so different from our offer. It looks to us that DOD really wanted termination. We don't want to give up trying, however, some key issues remain such as contingent deferral of the hit.

McDONNELL: -- Let me explain--regarding our offer of taking a contingency in part, if we can't do that we need to take the whole hit on the books which puts our companies in jeopardy.

YOCKEY: -- I understand from an accounting standpoint. Let me respond--what we tried to do was not give you specific instructions on how to respond. It is not our intent to terminate, but as was stated in the cure notice you are in trouble on this contract. We are open to your approach. You addressed equity--we don't believe we have a problem of that magnitude. I will be quick to tell you this is my opinion, not

SecDef's position.

McDONNELL: -- You're saying 70% of burden is ours and that's not equitable.

YOCKEY: -- You have an alternative to pursue claims.

McDONNELL: -- That still leaves open the issue of the contract which is not valid.

YOCKEY: -- Without prejudicing anyone's rights, reforming the contract under 85-804 is a separate problem.

ANDERS: -- In our view your proposal is not equitable.

YOCKEY: -- OK, we'll take your position.

McDONNELL: -- We wanted to use this meeting to see if we can adjust the proposal, for example, regarding the issue of contingent deferrals--we could give a bigger number. The second issue is on the 70/30 split--do we have to take the majority of the hit.

YOCKEY: -- We will consider anything, my own personal view is that

there are 3 parties to this.

ANDERS: -- We are a team.

YOCKEY: -- We haven't been able to evaluate claims so we can't say what the real share line would be.

McDONNELL: -- What if we don't give up claims?

YOCKEY: -- We will consider that--I do have a little trouble with this.

CANN: -- It's important to establish the frame of reference for the solution.

McDONNELL: -- We are trying to find the most likely to succeed solution.

YOCKEY: -- I can't say all the rationale for my position-you can assign a realistic expectation to the value of your claims but it's not dollar for dollar.

ANDERS: -- Beyond that the contract is lousy.

YOCKEY: -- The Fixed Price contract is your problem: I won't say Fixed Price is bad.

ANDERS: -- Regarding Fixed Price contracts, the issue is how it is applied not Fixed Price in itself. I'm talking about delivering state of the art development projects, it doesn't work. This puts us in an adversarial position with the customer from the start. It doesn't work.

ANDERS: -- I'm convinced we both made a mistake.

YOCKEY: -- You can find plenty of people who wanted Fixed Price contracts.

O'DONNELL: -- What are the other points?

McDONNELL: -- How hard is the $2B number?

YOCKEY: -- I'd like it better if it were $3B.

ANDERS: -- Why is $3B better than $2B, are we looking for blood?

YOCKEY: -- No, we gave you a show cause and you are deficient. We believe we have an enforceable contract. You want to change all parts of the contract and we will

entertain your proposals. Its easier to reform a contract without a fixed dollar value-- the government must get consideration and that goes in my calculations.

CANN: -- It's clear there is an advantage to the Navy for management of a cost type contract.

YOCKEY: -- You can make changes to a fixed price contract.

McDONNELL: -- We are trying to come up with a solution. As we see it, we would terminate vice jeopardize our companies.

YOCKEY: -- Fundamentally we are at the point where you should put your best proposal together and we will consider it and take it forward.

DEPARTMENT OF THE NAVY
NAVAL AIR SYSTEMS COMMAND
NAVAL AIR SYSTEMS COMMAND HEADQUARTERS
WASHINGTON, DC 20361

4200 AIR-02
7 January 1991

CERTIFIED MAIL - RETURN RECEIPT REQUESTED

Mr. George Kostohryz
Vice President, Contracts
GENERAL DYNAMICS
FORT WORTH DIVISION
P.O. Box 748
Fort Worth, TX 76101

Mr. Roger J. Witte
Vice President, Contracts and Pricing
MCDONNELL DOUGLAS
MCDONNELL AIRCRAFT COMPANY
P.O. Box 516
St. Louis, MO 63166

Dear Gentlemen:

General Dynamics Corporation and McDonnell Douglas Corporation (hereafter Team) are in default of Contract N00019-88-C-0050 dated 13 January 1988. The Government, therefore, is terminating Contract N00019-88-C-0050 in accordance with FAR Clause 52.249-8, "Default (Fixed-Price Supply and Service)" and 52.249-9,

"Default (Fixed-Price Research and Development)." The Team's right to proceed further under Contract N00019-88-C-0050 is terminated immediately upon receipt of this letter.

This action is based on the Team's inability to complete the design, development, fabrication, assembly and test of the A-12 aircraft within the contract schedule and the Team's inability to deliver an aircraft that meets contract requirements. On 17 December 1990, the Navy informed the Team that it considered conditions under the contract to endanger performance and asked the Team to cure those conditions. Having carefully considered the Team's 2 January 1991 response, I conclude that the Team has failed to explain or cure those conditions, and that the Team is in default of the contract for having failed to make progress and not meeting contract requirements. The A-12 aircraft will not be delivered within the contract schedule nor will it meet the weight guaranty contained with the contract specification.

Upon direction of the Contracting Officer, the Government may require the Team to transfer title and deliver to the Government any (1) completed or partially completed work not previously delivered to and accepted by the Government and (2) other property, including contract rights, specifically produced or acquired for the terminated portion of this contract. Such terminated supplies or services will be purchased against the Team's account.

The Government may acquire, under terms and in the manner the Government considers appropriate, work similar to the work terminated. The Team will be liable to the Government for any excess reprocurement costs, the Government reserves all rights and remedies provided by law or under Contract N00019-88-C-0050.

This is the final decision of the Contracting Officer. The Team may appeal this to the Armed Services Board of Contract Appeals. If the Team decides to appeal, the Team must, within 90 days from the date the Team receives this decision, mail or otherwise furnish written notice to the Armed Services Board of Contracting Appeals and provide a copy to the Contracting Officer from whose decision the appeal is taken. The notice shall indicate that an appeal is intended, reference this decision, and identify the contract by number. Instead of appealing to the Armed Services Board of Contract Appeals, the Team may bring an action directly in the U.S. Claims Court within 12 months from the date the Team receives this decision.

/s/ W.R. Morris
W.R. Morris
RADM, SC, USN
Contracting Office

326 003 2487

APP. 18.290

BEST AVAILABLE COPY

General Dynamics Corporation and McDonnell Douglas Corporation (hereafter Team) are in default of Contract N00019-88-C-0050 dated 13 January 1988. The Government, therefore, is terminating Contract N00019-88-C-0050 in accordance with FAR Clause 52.249-8, "Default (Fixed-Price Supply and Service)" and 52.249-9, "Default (Fixed-Price Research and Development)." The Team's right to proceed further under Contract N00019-88-C-0050 is terminated immediately upon receipt of this letter.

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DEPARTMENT OF THE NAVY
NAVAL AIR SYSTEMS COMMAND
NAVAL AIR SYSTEMS COMMAND HEADQUARTERS
WASHINGTON, DC 20361

AIR-OOC/MAO/mao
7 January 1991

MEMORANDUM FOR THE CONTRACT FILE

Subj: TERMINATION FOR DEFAULT OF CONTRACT N00019-88-C-0050

Contract N00019-88-C-0050 was awarded to the team of General Dynamics Corporation, Fort Worth Division, and McDonnell Douglas Corporation, McDonnell Aircraft Company, on January 13, 1988, for the design, development, fabrication, assembly and test of the Advanced Tactical Aircraft (A-12). After considering the factors set forth in Federal Acquisition Regulation 49.402-3(f), I have determined to terminate this contract for the default of the Contractor. The reasons for this action are as follows:

The terms of the Contract and applicable laws and regulations. Line Item 0005 of Contract N00019-88-C-0050 requires the team to design, develop, fabricate, assemble and test eight (8) A-12 aircraft to meet the requirements of Detail Specification SD-574-1. Among the requirements of SD-574-1 is the following significant performance guarantee: a weight empty proposed by the team in its offer to perform the full-scale development

contract. The contract as awarded required the team to deliver the first aircraft in June 1990. On August 17, 1990, after the team failed to meet that requirement and refused to agree to a new schedule, the Contracting Officer, based on information provided by the team, unilaterally established a new and reasonable schedule for the development aircraft. Modification P00046 established a new schedule for the first aircraft of December 1991 with the remaining seven aircraft to be delivered through 1992 to February 1993.

In addition to the full-scale-development obligations of the basic contract, the team competed for and accepted the risk of ceiling priced options for three years on pilot and low rate production. Each of the options after the first is conditioned upon the Navy's exercise of the prior year option at a quantity meeting the minimum specified for that year. Each option is also conditioned upon the Navy providing a specified amount of advance procurement funding at stated times in advance of the exercise of each option. On May 31, 1990, the Navy exercised the option for the first pilot production lot at a quantity of six aircraft to be delivered from June 1991 through May 1992 at a rate of approximately one every two months. The Navy has also provided the contractually specified funding to protect the option for the second production lot.

Contract N00019-88-C-0050 was awarded following competition; and award of the contract

violated no law or regulation.[1] No laws or regulations require the Navy to acquire the A-12 aircraft, or to acquire such an aircraft from the team.

The contract includes the clause entitled "Default", which can be found at FAR 52.249-9; and this clause, at paragraph (a)(1)(iii), provides that the contract may be terminated for default if the contractor so fails to make progress as to endanger performance of the contract. As outlined below, the Contractor's performance evidences an inability or unwillingness of this contractor to meet the requirements of the contract.

The specific failure of the Contractor and the excuses for the failure. In June 1990, the team informed the Navy that all of its obligations to develop and test A-12 aircraft could not be met.

In the months following this announcement, the team and the Navy conducted independent reviews of the development program, and engaged in

[1] In its "Memorandum In Support of Request for Contract Restructure," the team contended that the Navy violated Section 8118 of the Fiscal Year 1988 DoD Appropriations Act (P.L. 100-202) when it awarded a fixed-price type contract. That section required the Under Secretary of Defense to determine the program risk had been reduced to the point that realistic pricing could occur and that the contract type permits an equitable allocation of the risk. This determination was a precondition of any obligation of funds for full-scale development under a fixed-price type contract. The Under Secretary of Defense executed the appropriate determination prior to award of the A-12 contract.

extensive and intensive discussions about the effect of the delays on the future of the program and its affordability. During the course of these discussions, the team proposed that the Navy abandon its fixed-price contract and assume the cost risk of the team's performance. At the same time, the team insisted on relief from performance requirements of its development contract. In support of its proposal, the team submitted a lengthy memorandum of argument that all its performance difficulties were excusable.

On December 17, 1990, as a result of its reviews and growing concern about the progress of discussions with the team, the Navy notified the team that its failure to fabricate parts in time to permit timely delivery of the development and Lot I aircraft endangered performance of the contract, and informed the team that it had 10 days to cure the conditions endangering performance or explain the failure. This "cure notice" also informed the team that its failure to meet specified aircraft weight jeopardized the carrier suitability of the team's design. The team responded to the cure notice with an acknowledgment that it would not meet delivery schedules or certain specifications, a brief description of its progress under the contract, and a reference to its previously submitted arguments. After thorough review, I have concluded that the explanation and argument do not justify excusing the team from its contract obligations to deliver conforming aircraft on time. The team has made no case that three to nine months further delay in the delivery of the first aircraft or two or more years' delay in the completion

of development is other than the team's fault, or that it is entitled to be relieved of the performance requirements of its contract.

Specifically, the team cannot deliver the first prototype aircraft required by Line Item 0005 in December 1991. Since June 1990, the team has consistently reported its delays; and the Navy independent review confirmed that, given the state of the team's development efforts, delivery of aircraft and completion of related contract requirements could occur no sooner than.

The importance of this delay cannot be overstated. The production options must be exercised by dates certain to be enforceable. As a consequence of the team's delay, the Navy would be required to purchase production aircraft before verifying that the aircraft are operationally suitable and effective. While the contract places the risk of defects on the contractor, that is small comfort if major redesign is necessary. Moreover, the delay so increases the cost to the team of completing the contract that it casts doubt on their willingness to perform.

Specifically, the team cannot meet the performance requirements of the contract. The team is currently designing the aircraft to have a weight empty 7930 pounds in excess of the guaranteed contract weight empty. This additional weight precludes the team from meeting contract requirements for takeoff distance, cruise specific

range, maximum airspeed, and fuel flow, all of which directly affect mission capability.

Excuses offered by the team are as follows. First, the team contends that its development and manufacturing activities have been substantially affected by acts and omissions of the Government. Specifically, the team alleges that the Government failed to provide "very important information vital to the performance of the contract" that was available to the Government. Second, the team alleges that necessary risk reduction prior to the award of a fixed price development contract was not present in this effort. Intertwined is the argument that meeting the required weight called for by the specification is impossible. Third, the team argues that its obligation to perform is limited to the amount of funds available, provided through incremental Government funding. Finally the team argues that the schedule is not valid and is unreasonable because it purports to schedule FSD aircraft deliveries after delivery of Lot I aircraft.

The Government has provided the team all information relevant to the performance of this contract that the Government was required contractually to provide. The team has alleged that the Government had superior knowledge of certain information, that was vital to the contractor, yet did not disclose that information. The team, however, has failed to specify what information was withheld that affected its ability to perform and the legal duty of the Government to disclose this information.

The Government believes that the contract is valid and that risk was reduced sufficiently to award a fixed price development contract. The weight guaranty in the contract specification was provided by the team. The team is currently projecting weight at 7930 pounds over the required weight which critically calls into question the aircraft's suitability for carrier operations. The added weight impairs the aircraft's single engine rate of climb and increases substantially wind over deck requirements; both serious considerations for carrier operations. The team has provided no valid excuse for not meeting the contract weight that it submitted and agreed to meet.

This contract is a fixed price contract that requires delivery of conforming goods by a date certain conditioned on the Government allotting funds in the amounts and at the times stated. It is not a cost type of contract where the contractor is only required to work to the limit of available funds.

Finally, the overlapping schedule of FSD and Lot I deliveries does not relieve the team of the requirement to meet either schedule. The FSD schedule was extended after the team failed to meet the original schedule in the contract. The Lot I schedule could not be extended at the same time because too much uncertainty surrounded the team's ability or willingness to perform to any schedule.

In summary, the team's failure to make progress and to deliver an aircraft meeting required weight has placed the entire program in jeopardy; and the contractors have offered no adequate excuse for these failures.

The availability of the supplies or services from other sources. The A-12 in the configuration proposed by the team is probably available only from the team.

The degree of essentiality of the contractor in the Government acquisition program and the effect of a termination for default upon the contractor's capability under other contracts. McDonnell Douglas Corporation is the sole source for the F/A-18, the F-15, the AV-8, the T-45, the AH-64, the C-17 and several other weapon systems. General Dynamics is the sole source for the F-16, the Trident submarine, the M-1 tank and several other weapon systems. Both companies have an unknown number of classified programs.

Under the terms of the contract, both companies are jointly and severally liable for all obligations of the contract. To date, the government has obligated $3.5B under the FSED Line Items, $1.2B under the Lot I line items and $185M under the Lot II line items. Payments to date are $2.6B, $101M and $4M for FSED, Lot I and Lot II, respectively for a total of $2.7B. The government has accepted several line items with a value of approximately $1.2B. The team's current

termination liability is approximately $4B for FSED, $600M for Lot I and $180M for Lot II. If this contract were completed, estimates of the costs at completion range from $1B to $10B over the contract ceiling price. Because approximately $1.2B worth of effort has already been accepted, the government would be able to demand repayment of $1.2B of the $2.4B already paid to the teams. Subcontractor and Government claims for payment could well imperil both companies' ability to perform other contracts.

The effect of a termination for default on the ability of the contractor to liquidate guaranteed loans, progress payments, or advance payments. There is no reason to believe that the contractor will be able to repay the progress payments under this contract.

Any other pertinent facts or circumstances. The team has recently submitted another version of its arguments to support restructure of the contract. Presidents of both companies provided qualified certifications of the "claim" (each certified only its own costs). Preliminary review supports the conclusion that the claim has no merit and, because of the flawed certification, cannot be considered under the Contract Disputes Act.

In addition, the team has requested reformation of the contract under P.L.85-804 but has not persuaded anyone to exercise that authority to restructure the contract. Moreover, this is solely

within the discretion of the agency head, and is not subject to appeal.

/s/ W. R. Morris
W. R. Morris
RADM, SC, USN
Assistant Commander
for Contracts

MCDONNELL DOUGLAS CORPORATION

29 January 1991

To: Eleanor Spector

From: Herb Lanese

As discussed during our telephone conversation this afternoon, I have attached three documents:

1) A representation letter from our Treasurer, Mr. J. W. Chase, giving his opinion that the "material adverse change" issue under our current revolving credit agreements that we discussed would be resolved upon receipt of a deferment letter. In addition, he represents that we are pursuing aggressively all available financing alternatives to ensure that our corporation has enough funding to meet its growth needs and obligations.

2) A copy of the deferment request letter and the deferred payment agreement that we left with Rear Admiral W.R. Morris at our meeting with him on Wednesday, 16 January 1991. These will be signed by McDonnell Douglas Corporation and General Dynamics Corporation upon receipt of a demand letter.

I hope this addresses the issues you raised during our telephone conversation and appreciate in advance your prompt consideration.

/s/ Herbert J. Lanese
Herbert J. Lanese
Senior Vice President-Finance

Memo No. JWC-447
29 January 1991

TO: H. J. Lanese

SUBJECT: MDC Borrowing/Credit Arrangements

1. Certain of our key banks are concerned that the termination of the A-12 may have resulted in a "material adverse change" in MDC's financial condition. As you are aware, if the banks invoke the material adverse change provisions in our revolving credit agreements, we cannot borrow any additional amounts under those agreements. At risk is $190M currently not drawn under our $750M agreement. The chief concern of the banks is that the Navy will submit a demand letter and then not respond favorably to a request for deferment. In my opinion, if the Navy were to provide such a deferment, this cloud of material adverse change would be dissipated and MDC would have full access to the remaining $190M currently undrawn under the $750M revolving credit agreement.

2. We are pursuing aggressively all available financing alternatives, including sale of real properties, sale and sale/leaseback of real and personal properties, and expansion of our asset-backed program. Further, we will issue public and/or private debt if either or both of those markets again become economically accessible for MDC securities, and it is our intent to negotiate new bank credit facilities as soon as feasible.

/s/ J. W. Chase
J. W. Chase
Treasurer

MCDONNELL DOUGLAS CORPORATION
ST. LOUIS, MISSOURI

GENERAL DYNAMICS CORPORATION
ST. LOUIS, MISSOURI

January , 1991

W.R. Morris
Rear Admiral, SC, U.S. Navy
Contracting Officer
Department of the Navy
Naval Air Systems Command
Naval Air Systems Command Headquarters
Washington, D.C. 20361

Re: Contract N00019-88-C-0050 - A-12 Program
Request for Deferred Payment Agreement

Dear Admiral Morris:

This will acknowledge your letter of January , 1991, initiating a demand for repayment of unliquidated progress payments in accordance with subpart 32.6 of the Federal Acquisition Regulation.

In accordance with FAR 32.613, this will constitute a request by the Contractor Team for deferment of collection. The basis for this request is:

(a) immediate payment of the amount demanded is not practical; and

(b) the amount is disputed.

While the Team has not yet filed a notice of appeal or complaint, such a filing is intended.

We believe that the Team members, as well as prior audits performed by the Department of Defense, have established that repayment at this time is not practical; that such repayment would impair their continued operations, and more particularly those operations under national defense contracts. In support of these representations, each team member is providing financial data for its respective company.

This will serve as our request for a deferred payment agreement in accordance with the terms of FAR 32.613. The Team has prepared a proposed agreement which is attached. We are prepared to execute such agreement at your earliest convenience. We are also prepared to meet with you to discuss this subject.

Sincerely,

MCDONNELL DOUGLAS CORPORATION
James C. Restelli
Vice President
Business Operations, MCAIR

GENERAL DYNAMICS CORPORATION
D. Blaine Scheideman
Corporate Vice President
Contracts, Pricing and International Offset

DEFERRED PAYMENT AGREEMENT

This Agreement is entered into as of this day of January, 1991 between the United States of America represented by the U.S. Navy Accounting and Finance Center, Department of the Navy (hereinafter called the "Government"), and General Dynamics Corporation and McDonnell Douglas Corporation (hereinafter collectively called the "Team").

WHEREAS, by final decision dated January 7, 1991, the Government terminated Contract No. N00019-88-C-0050 for default; and

WHEREAS, the Team intends to appeal or file suit on said final decision within the time limits set forth therein; and

WHEREAS, by letter dated , 19_, the Government made a demand upon the Team for repayment of progress payments made under Contract No. N00019-88-C-0050 in the amount of $; and

WHEREAS, the Government, pursuant to the provisions of Federal Acquisition Regulation, subpart 32.6, has determined as appropriate the request of the Team for deferral of collection action on the claim, and, accordingly, it is mutually agreed that collection of the Government's demand be deferred on the conditions and terms stated below.

NOW, THEREFORE, the parties hereto agree as follows:

(1) Indebtedness. The Team acknowledges that the principal sum of $ represents the amount of the debt alleged to be due the Government from the Team under Contact No. N00019-88-C-0050.

(2) Claim Deferment. Conditioned on the Team's diligent prosecution of the appeal or suit, the Government will take no action, except as otherwise hereinafter provided, to enforce collection of the aforementioned demand pending: (a) a decision by the Board or U.S. Claims Court and, if appealed by either party, the Court of Appeals for the Federal Circuit; or (b) a negotiated settlement arrangement by and between the Government and the Team without such decision.

(3) Interest. The Team shall pay interest to the Government at the rate set, from time to time, by the Secretary of the Treasury pursuant to P.L. 92-41 per annum on the amount determined due (a) upon the decision of the Board or Court unless modified on appeal (less any prepayment made under paragraph (5) below); (b) upon agreement if negotiation results in a settlement prior to decision by the Board or Court; (c) upon any prepayment made under paragraph (5); or, (d) upon any default under paragraph (6) below, which interest shall accrue and be payable from , 19__, until the date payment is received.

(4) Submission of Data. Each Team member agrees to separately submit to the Government periodic financial statements as appropriate and to submit such other pertinent

reports and information as may be required by the Government pursuant to Federal Acquisition Regulation, subpart 32.6.

(5) Prepayment. The Team may at its option at any time before a final resolution of the dispute, notwithstanding the deferral of collection by this Agreement, pay to the Government all or any part of the amount stated in the Government's demand letter.

(6) Default. Upon failure by the Team to pursue diligently the appeal before the Board or Court, the Government shall then have the right, upon written notice to the Team, to require immediate payment of the claim stated by the Contracting Officer, plus accrued interest in accordance with paragraph (3) above. In the event the Government does not exercise its right to require immediate payment, such forbearance shall not be construed as a waiver of the Government's right to do so, or as an approval of the Team's act, acts, or failure to act. If, prior to the final disposition of the entire dispute or payment in full in the event of a negotiated settlement, the Team members are adjudicated bankrupt, or liquidation proceedings are commenced, the amount stated in the Government's demand letter, plus accrued interest pursuant to paragraph (3) above, shall become immediately due and payable without notice by the Government.

THEREUPON, the Government's right to immediate payment under the terms of this Agreement includes any available legal remedy deemed necessary for the satisfaction of the unpaid

claim including accrued interest at the rate specified in paragraph (3) above. Nothing in this Agreement shall be construed as a limitation, or waiver of any right, remedy or defense which the Team or the Government could otherwise advance under the appeal to be filed before the Board or Court.

(7) Payment. Within a reasonable time after the date of the final decision by the Board or Court, or upon exhaustion of any appeals therefrom, or upon settlement of this matter by and between the Team or a member of the Team and the Government prior to such decision, payment of both the principal amount and interest thereon, if any, determined to be due the Government will be made by the Team or a member of the Team as appropriate. All payments shall be made by check drawn payable to the "Department of the Navy" and forwarded to the following address:

IN WITNESS WHEREOF, the parties have executed this Agreement as of the day and year first above written.

THE UNITED STATES OF AMERICA

By:

ATTEST:

GENERAL DYNAMICS
CORPORATION

By:

MCDONNELL DOUGLAS
CORPORATION

By:

DEPARTMENT OF THE NAVY
Naval Air Systems Command
Naval Air Systems Command Headquarters
Washington, DC 26361

In Reply Refer To
05 February 1991

Mr. George Kostchryz
Vice President, Contracts
General Dynamics Corporation
Fort Worth Division
P.O. Box 748
Fort Worth, TX 76101

Mr. Roger Witte
Vice President, Contracts and Pricing
McDonnell Douglas Corporation
McDonnell Aircraft Company
P.O. Box 516
St. Louis, MO 63166

Dear Gentlemen:

On 7 January 1991, the government terminated Contract N00019-88-C-0050 due to the Contractors' default. The progress payment clause of the contract provides that the Contractors shall, on demand, repay the Government the amount of unliquidated progress payments. Subpart 32.6 of the Federal Acquisition Regulation requires the Contracting Officer to take prompt action to collect contract debts such as this. This letter constitutes

the government's demand for payment of unliquidated progress payments under the contract.

The amount payable to the Government on account of unliquidated progress payments is $1,352,459,644.00. Payment is to be made by check made available to the "Department of the Navy" and forwarded to the following address:

Comptroller of the Navy
Room 4E768, The Pentagon
Washington, DC 20350

Any portion of this amount not paid within 30 days from the date of this letter shall be subject to interest at a rate established by the Secretary of the Treasury, for the period affected, under 50 U.S.C. App. 1215(b)(2). If, in the future, additional amounts are determined to be due the Government by reason of the default, we will make demand for payment of those amounts at that time.

The Contractors have the right to inspect and copy agency records pertaining to the debt, to obtain review within the agency of the determination of this indebtedness, and an opportunity to make a written agreement with the head of the agency to repay this debt. The Contractors may also submit a request for deferment of the collection if immediate payment is not practical or if the amount is disputed. Any such requests should be forwarded to Rear Admiral W.R. Morris, SC, USN, Assistance Commander for Contracts, Naval Air Systems Command, who has been designated the responsible official for

determining the amount of this debt and for its collection.

Sincerely,

/s/ W.R. Morris
W.R. Morris
Rear Admiral, SC, USN
Assistant Commander for
Contracts

DEFERMENT AGREEMENT

This Agreement entered into as of 5 February 1991, between the United States of America (hereinafter called the "Government") and General Dynamics Corporation and McDonnell Douglas Corporation, McDonnell Aircraft Company (hereinafter called the "Contractors") having principal places of business at Fort Worth Division, P.O. Box 748, Fort Worth, Texas 76101 and P.O. Box 516, St. Louis, Missouri 63166, respectively.

WHEREAS, the Contracting Officer, Naval Air Systems Command, Arlington, Virginia, by Certified Letter dated 5 February 1991, demanded payment of $1,352,459,644.00 arising out of the default of the Contractors under contract N00019-88-C-0050;

WHEREAS, the Contractors represent that they will appeal to the Armed Services Board of Contract Appeals or file suit in the Claims Court on the Contracting Officer's final decision within the time limits set forth therein;

WHEREAS, the Contractors, by a letter dated 5 February 1991, requested that government collection action regarding the amount demanded by the Contracting Officer be deferred pending the outcome of the Contractors' appeal or suit;

WHEREAS, the Contractors have made a showing to the Department of Defense that, absent deferment, one or both Contractors may be placed in

a financial condition that would endanger essential defense programs;

WHEREAS, the Contractors are jointly and severably liable under the contract and the Department of Defense has determined that it is not in the best interest of the Government to have either of the Contractors in a financial condition that endangers essential defense programs;

NOW, THEREFORE, the parties agree that collection of the Government's claim will be deferred subject to the following terms and conditions;

(1) Indebtedness. The Contractors acknowledge that the principal sum of $1,352,459,644.00 represents the amount demanded by the Government under Contract N00019-88-C-0050. The Contractors disagree that any amount is due to the Government.

(2) Deferment. The government will take no action, except as otherwise hereinafter provided, to enforce collection of the amount demanded pending (a) a decision by the Armed Services Board of Contract Appeals or the Claims Court on the Contractors' appeal, or (b) a negotiated settlement by and between the Government and the Contractors without such decision. The statute of limitations for collection of this debt will be suspended while awaiting a decision of dismissal from the Board or the Claims Court.

(3) Interest. The Contractors shall pay interest to the Government at the rate established by the Secretary of the Treasury as provided in Section 12 of the Contract Disputes Act of 1978 (Public Law 95-563). The rate is adjusted each January and July by the Secretary of the Treasury and shall apply to the amount determined due upon (a) decision by the Board or the Claims Court (less any prepayments made under paragraph (4) below); (b) a negotiated settlement; or (c) a default under paragraph (5) below. Such interest shall accrue and be payable from 5 February 1991 until the date of receipt of such payment.

(4) Prepayment. The Contractors may at their option, at any time before the Board or the Claims Court renders its decision, notwithstanding the deferment of collection by this Agreement, pay to the Government all or any of the amount determined to be due by the Contracting Officer's decision. Any prepayments hereunder shall be without prejudice to the Contractors' rights under their appeal before the Board or the Claims Court. Prepayments and related interest will be adjusted if the amount of the prepayment is at variance with the decision of the Board or the Claims Court or if settlement is agreed to at some different principal amount without decision of the Board or the Claims Court.

(5) Default. The Government shall have the right to require immediate payment of the principal sum of $1,352,459,644.00, plus accrued interest in accordance with paragraph (3) above, should any of the following events of default occur:

(a) failure to appeal to the Armed Services Board of Contract Appeals or file suit in the Claims Court on the Contracting Officer's final decision within the time limits set forth therein, (b) failure by the Contractors diligently to pursue resolution of their appeal to the Armed Services Board of Contract Appeals or their suit in the Claims Court, or (c) appointment of a trustee, receiver or liquidator for all or a substantial part of either Contractor's property, or institution of bankruptcy, reorganization, arrangement of liquidation proceedings by or against either Contractor. In the event the Government does not exercise its right to require immediate payment, such a forbearance shall not be construed as a waiver of the Government's right to do so, or as an approval of the act, or a failure to act, that constituted the default.

(6) Access to Records. The Contractors agree to submit any financial information requested by the Government, and for reasonable access to the Contractors' records and property by Government representatives. These requirements apply equally to the Contractors' commercial business as well as government business.

(7) Financial Responsibility. The Contractors and their respective successors-in-interest agree to maintain sufficient assets or available credit to pay the Government the full amount of the debt. Upon request, the Contractors or their successors-in-interest agree to provide the Government documentation that evidences, to the

satisfaction of the Government, compliance with this requirement.

(8) Waiver. Nothing in this Agreement shall be construed as a limitation, or waiver of any right, remedy or defenses which the Contractors or the Government could otherwise advance in any legal action.

(9) Payment. Within thirty (30) days after the date of the decision by the Board or the Claims Court, or upon settlement of this matter by and between the Contractors and the Government prior to such decision, payment of the principal amount and interest determined to be due the Government will be made by the Contractors. All payments shall be made by check drawn payable to the "Department of the Navy" and forwarded to the following address:

Comptroller of the Navy
Room 4E768, the Pentagon
Washington, D.C. 20350

(10) Applicability. The terms of this Agreement apply to the Contractors and their successors-in-interest jointly and severably.

(11) Terms of Agreement. This Agreement shall remain in full force and effect as set forth herein, subject to review on force and effect as set forth herein, subject to review on 1 December 1992 and annually thereafter. Notwithstanding any other provision of this Agreement, this Agreement may be terminated after such review if the Government

determines (within its sole discretion) that (a) either of the Contractors has failed diligently to pursue resolution of their appeal to the Armed Services board of Contract Appeals or their suit in the Claims Court, or (b) there is a substantial change in either Contractors' financial condition such that deferment is no longer in the best interest of the Government. Such termination shall be effective 30 days after written notice is provided.

IN WITNESS THEREOF, the parties hereto have executed this Agreement as of the day and Year first above written.

THE UNITED STATES OF AMERICA

By: /s/ Robert McCormick
Assistant Secretary of the Navy

GENERAL DYNAMICS CORPORATION

By: /s/Donald W. Putham

Name: /s/ Name and /s/ Donald W. Putham

ATTEST: Title: Corporate Director of Contracts

MCDONNELL DOUGLAS CORPORATION

By: /s/ J.M. Garoner

Name: /s/

Name and /s/ J.M. Garoner

ATTEST:

Title: Staff V.P. Contracts & Pricing

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs	)	No. 91-1204C
v.	)	
UNITED STATES OF AMERICA,	)	Filed: February 20, 1992
Defendant.	)	

OPINION AND ORDER

HODGES, Judge.

This case comes before the court on defendant's motion to dismiss for lack of jurisdiction. We find that plaintiffs' claims and defendant's termination for default are properly before this court for the reasons stated below. Defendant's motion to dismiss is therefore denied in part.

FACTS

In 1984, the Department of the Navy introduced the Advanced Tactical Aircraft Program (A-12) to

develop a carrier-based, low observable (Stealth) attack aircraft. The Navy asked four defense contractors to form teams to compete for the A-12 Studies and Full Scale Engineering Development contracts. These contractors included McDonnell Douglas Corporation and General Dynamics Corporation (plaintiffs), who agreed to bid for the contracts as a team.

Plaintiffs' November 2, 1984 Teaming Agreement provided that the contractors would respond jointly to A-12 Requests for Proposals. The parties also agreed to an integrated organizational system to manage and allocate A-12 work equally.

The scope of the teaming relationship was described in Section 10:

> 10. Teaming Relationship
>
> 10.1 This Agreement provides exclusively for a teaming relationship and related technology exchange with respect to the [A-12] System and variants or derivatives thereof, specifically including other new tactical aircraft designed for substantially the same mission roles and performance requirements, and the correlative rights and duties of the Parties. . . . This Agreement is not intended to and shall not in any way abridge, limit or restrict the rights of either Party to pursue, either independently or in conjunction with any

> other person or entity, business opportunities relating to products other than the System, including products in competition with the System. *This Agreement does not constitute and shall not be construed or given effect as a joint venture, partnership, pooling arrangement, or other formal business organization, or as creating any fiduciary relationship.* Except as expressly provided herein, nothing herein shall be construed as providing for the sharing of profits or loss, nor shall either Party be liable to the other for any of the costs, expenses, risks, or liabilities arising out of the other's activities in connection with the performance of programs outside this agreement. (emphasis added)

Plaintiffs submitted a joint proposal for the A-12 Full Scale Engineering Development contract, and were awarded the contract in January 1988. Plaintiffs' representatives executed a single contract to bind their respective corporations. The contract contained standard terms, but a special provision was inserted to hold the team members responsible for their actions:

> H-44 JOINT AND SEVERABLE LIABILITY
>
> If this contract is awarded to contractors whose contractual relationship with the

> government will be as a team, this clause shall apply. McDonnell Aircraft Company and General Dynamics Fort Worth Division shall be jointly and severably liable for all obligations of this contract. It is specifically agreed that the liability of the parties to the Government under this contract shall not be limited by any provision of the Teaming Agreement relating to the division of responsibility or by any other provision of the Teaming Agreement.

The contract required that team members have the capacity to produce the aircraft independently and to compete against each other in production.

Problems developed during performance, and plaintiffs requested that the contract be restructured. Instead, the Navy issued plaintiffs a cure notice on December 17, 1990. On December 31, plaintiffs submitted equitable adjustment requests totalling $ 1,401,181,205. The requests did not demand a Contracting Officer's final decision "in light of on-going discussions and the mutually perceived desire to restructure the program."

The requests included two certifications, one from each contractor. The president of General Dynamics Corporation signed one of the certifications:

CERTIFICATE

> Herbert F. Rogers, the Senior General Dynamics Corporation official in charge at the General Dynamics Fort Worth Division, hereby certifies, that this claim is made in good faith, the supporting data are accurate and complete to the best of the company's knowledge and belief, and the amount requested accurately reflects the contract adjustment, under the A-12 FSD contract and/or a contract implied-in-fact, for which the company believes the government is liable. This certificate extends only to those elements of the claim as to which General Dynamics has estimated a pricing impact, and neither company certifies to the pricing of amounts for which the other company has estimated the government is liable.

Mr. G. A. Johnston signed the second certification, and identified himself as "the Senior McDonnell Douglas Corporation official in charge at McDonnell Aircraft Company." The body of the second certification duplicated that submitted by General Dynamics.

The Contracting Officer issued a January 7, 1991 decision terminating the contract for default. The decision was designated "final" and included a disclosure that plaintiffs could appeal to this court within 12 months. The decision was followed by a February 5, 1991 letter demanding return of $ 1,352,459,644 in unliquidated progress payments as

a result of the termination. The Navy demanded payment by check and stated that interest would begin to accrue after 30 days.

The letter informed plaintiffs of their administrative rights to obtain a review of their indebtedness and "an opportunity to make a written agreement with the head of the agency to repay this debt." The letter did not advise plaintiffs of their appeal rights pursuant to the Contract Disputes Act of 1978 (CDA), *41 U.S.C. §§ 601-613 (1988).*

On the day the demand letter was issued, plaintiffs contested the demand for return of progress payments and signed a Deferment Agreement with the Navy. The agreement described the demand as a government claim, and acknowledged plaintiffs as individual contractors responsible for the payments. Representatives of the contractors signed the agreement on behalf of their respective corporations.

On February 18, 1991, plaintiffs advised the Government that their December 31, 1990 requests were claims which had been constructively denied by the Navy's decision to terminate the contract. If plaintiffs' claims were not denied, the team requested a Contracting Officer's decision.

The Contracting Officer advised plaintiffs on February 22, 1991 that the certifications attached to their December 1990 requests were defective because either the team or each team member should have certified the claims. The Contracting Officer further

noted that plaintiffs' certifying language was "impermissibly qualified and vague."

Defendant informed the contractors of another defect in their submission on May 16, 1991: "You have never furnished to the contracting officer, either with or without the required CDA certifications, a package containing the requisite factual detail and supporting documentation necessary to fulfil the statutory and regulatory requirements of a 'claim'."

Plaintiffs filed new certifications for their December requests on June 7, 1991. These were almost identical to those attached to their December requests. One certification was signed by the vice chairman of General Dynamics Corporation and the other by the president of McDonnell Aircraft Company. These officials also signed an alternative joint certification:

> **CERTIFICATE**
> [Joint Certification]
>
> Herbert F. Rogers, the Senior General Dynamics Corporation official in charge at the General Dynamics Fort Worth Division, and J. F. Capellupo, the Senior McDonnell Douglas Corporation official in charge at the McDonnell Aircraft Company, a Division of the McDonnell Douglas Corporation, hereby certify on behalf of the General Dynamics - McDonnell Douglas Aircraft A-12 Contractor Team, that this

> claim is made in good faith, the supporting data are accurate and complete to the best of the Contractors' knowledge and belief, and the amount requested accurately reflects the contract adjustment, under the A-12 FSED contract and/or a contract implied-in-fact, for which the Contractor Team believes the government is liable.

The alternative certification was intended to protect plaintiffs if the government's position were upheld.

Also on June 7, plaintiffs filed suit in this court pursuant to the Contract Disputes Act, *41 U.S.C. § 609(a) (1988).* Their complaint included the following requests for relief: (1) grant plaintiffs' December 31, 1990 equitable adjustment requests, (2) convert the termination for default to one for convenience, (3) deny defendant's demand for return of progress payments, (4) award performance costs and reasonable profit, (5) award settlement expenses, and (6) award damages for breach of contract.

Plaintiffs submitted to the Navy a $ 1,286,127,692 termination for convenience cost proposal on June 26, 1991, and amended it on July 26, 1991. Both proposals contained certifications identical to those submitted on June 7, 1991.

After receiving plaintiffs' requests, the Contracting Officer ruled that all of the certifications were defective. Furthermore, the protective joint

certifications of June 7, June 26, and July 26, 1991 were conditional and therefore invalid. In a letter dated August 5, 1991, the Contracting Officer advised plaintiffs that he would not consider their requests further because a complaint had been filed. No further action would be taken regarding these requests without direction from the court.

Defendant filed a motion to dismiss on August 7, 1991. On September 16, 1991, the court granted plaintiffs' motion for leave to file an amended complaint seeking termination for convenience costs as set forth in the contractors' June 26, 1991 cost proposal. On December 31, 1991, plaintiffs filed a notice pursuant to RUSCC 20(a)(1), advising the court that "McDonnell Douglas/General Dynamics Team" had been added to the suit as a plaintiff.

For the purposes of this Opinion, two factors determine whether this court may accept jurisdiction of any part of this case. These are (1) plaintiffs' December 31, 1990 equitable adjustment requests for $ 1,401,181,205 and (2) defendant's termination of plaintiffs' contract for default and its demand for return of unliquidated progress payments totalling $ 1,352,459,644.

DECISION

I.

Defendant opposes jurisdiction in the United States Claims Court alleging lack of privity, improper

certification, and insufficient supporting data. We address these issues as follows:

A. Privity

Defendant argues that the Teaming Agreement created an entity separate from the contractors. The team, not the contractors, signed the contract and later performed the work. Accordingly, only the team is in privity of contract with the Government. Without the team as plaintiff, defendant contends that the court lacks jurisdiction to proceed. *E.g., United States v. Johnson Controls, Inc.*, 713 F.2d 1541, 1550-51 (Fed. Cir. 1983) (privity of contract necessary under the CDA for a contractor to file a suit in this court); *accord Erickson Air Crane Co. v. United States*, 731 F.2d 810, 813 (Fed. Cir. 1984).

Defendant directs the court's attention to plaintiffs' joint Best and Final Offer submitted in accordance with the Federal Acquisition Regulations (FAR), 48 C.F.R. § 15.611(d) (1987): "Following evaluation of the best and final offers, the contracting officer . . . shall select that source whose best and final offer is most advantageous to the Government. . . ." (emphasis supplied). Defendant interprets this provision to require the award of a contract to a single entity.

Because the offer was submitted jointly, the Government contends that it contracted with the team entity, not individual corporations. It cites legislative history for the proposition that Congress

wanted government contracts to be administered through a "single point of contract approach" in order to expedite the resolution of disputes. S. Rep. No. 1118, 95th Cong., 2d Sess. 16-17, *reprinted in* 1978 U.S.C.C.A.N. 5235, 5250-51.

Defendant points to the FAR definition of a "contractor team arrangement" at *48 C.F.R. § 9.601 (1987)*: "(a) Two or more companies form a partnership or joint venture to act as a potential prime contractor; or (b) A potential prime contractor agrees with one or more other companies to have them act as its subcontractors under a specified Government contract or acquisition program." Defendant would include plaintiffs under one of these categories, requiring either the team or prime contractor to certify the claims.

In response, plaintiffs cite their Teaming Agreement and the contract to show that the Government signed a single contract with two independent prime contractors. Plaintiffs emphasize the fact that the contract called for competition between the team members to produce the aircraft after the development stage.

The record shows that the Navy specifically directed prospective contractors to form teams to compete for the A-12 contract. Plaintiffs joined in their Teaming Agreement to comply with the Navy's directive. The record includes no evidence that the Navy considered plaintiffs' agreement to be unsatisfactory or improper. The Teaming Agreement advised the

Government that plaintiffs' relationship did not create a joint venture or other formal business organization. It called for two prime contractors to work jointly on A-12 projects in a team effort pursuant to the Navy's directive.

Plaintiffs worked on the contract as equals and retained their corporate independence. No prime/subcontractor relationship existed. Accordingly, plaintiffs did not perform the contract under a "contractor team arrangement" as defined by the FAR. The definition of "contract" at *48 C.F.R. § 2.101 (1987)* sets no limitation on the number of prime contractors and nothing in the FAR prohibits the Government from contracting with two prime contractors.

The Joint and Severable Liability clause of the contract held plaintiffs accountable for their actions. The clause demonstrates the Government's understanding of the teaming relationship at the time the contract was awarded - two prime contractors working jointly to complete the job. Had the Government contracted with plaintiffs in a "team arrangement" as defined at *48 C.F.R. § 9.601 (1987)*, no such clause would have been necessary.

Plaintiffs were prime contractors, and they were in privity with the Government; it is not necessary for "The Team" to be a party. Plaintiffs properly filed suit in this court.

B. The December 31, 1990 Certifications

Defendant argues that plaintiffs' December 31, 1990 certifications are qualified and therefore defective. It also contends that the officers who certified the claims did not have authority to bind the team.

The Contract Disputes Act, *41 U.S.C. § 605(c)(1) (1988)*, requires a contractor to certify claims over $ 50,000: "The contractor shall certify that the claim is made in good faith, that the supporting data are accurate and complete to the best of his knowledge and belief, and that the amount requested accurately reflects the contract adjustment for which the contractor believes the government is liable." The certification requirements are jurisdictional and cannot be waived. *Thoen v. United States*, 765 F.2d 1110, 1116 (Fed. Cir. 1985).

Plaintiffs' certifications contained language which limited their applicability, in that each contractor certified only those elements for which it could estimate a pricing impact. Neither contractor certified the pricing of elements requested by the other contractor. Defendant interprets this as an attempt to evade the CDA requirement that a contractor should certify all portions of its claim.

A certification need not be embodied in a single correspondence. *See United States v. General Electric Corp.*, 727 F.2d 1567, 1569 (Fed. Cir. 1984) (contractor's certification which failed to include an assertion that the Government was liable, substantially complied with the CDA by making this

assertion in the attached documents). Each prime contractor certified its portion of the claims. The certifications together contained the necessary elements and made the assertions necessary for a proper certification.

Plaintiffs' corporate presidents had the authority to bind their respective corporations and they had the authority to certify the claims before the court. *48 C.F.R. § 33.207(c)(2) (1987).* No argument to the contrary has been made. Defendant merely stresses that the other party to its contract was a team entity. We do not agree.

Plaintiffs were dual prime contractors who certified their own pricing information in the claims. It would not have been proper for one contractor to certify data which was exclusively within the other's province. No provision of the CDA or its implementing regulations requires dual prime contractors to submit a joint certification to the Government. We hold that the certifications substantially complied with CDA requirements. *Id.* at 1569.

Defendant also argues that we lack jurisdiction to proceed because plaintiffs failed to submit an unconditional certification from an individual who could bind the team. We have ruled that the Teaming Agreement did not create a separate entity, so it is not necessary to address this argument further.

C. Sufficiency of the Supporting Data

Defendant's final attack on the December 31, 1990 claims lies in an obscure sentence found in a May 16, 1991 letter to the contractors. The Contracting Officer advised plaintiffs that their requests lacked sufficient supporting data to meet the CDA requirements of claims.

The Contract Disputes Act does not require a particular form for a claim to the Contracting Officer: "All that is required is that the contractor submit in writing to the contracting officer a clear and unequivocal statement that gives the contracting officer adequate notice of the basis and amount of the claim." *Contract Cleaning Maintenance, Inc. v. United States*, 811 F.2d 586, 592 (Fed. Cir. 1987) (citing *Tecom Inc. v. United States*, 732 F.2d 935, 936-7 (Fed. Cir. 1984)); *Metric Constr. Co. v. United States*, 1 Cl. Ct. 383, 392 (1983).

To determine whether a "claim" meets all of the CDA requirements, one must examine the entire submission. *Contract Cleaning*, 811 F.2d at 592; *see also R & R Enterprises*, ASBCA No. 41382, 91-2 B.C.A. (CCH) P23,707 at 118,677 ("adequate notice" requirement in *Contract Cleaning* requires the contractor to submit information "sufficient to enable the contracting officer to undertake a meaningful review of the claim").

Plaintiffs' December 31, 1990 requests notified the Contracting Officer of the basis for their claims and

they quantified the amounts. The requests gave the Contracting Officer enough information to conduct a meaningful review of plaintiffs' requests, and thus complied with the CDA.[1] *Contract Cleaning*, 811 F.2d at 592.

II.

Defendant opposes its own claim for return of progress payments because potentially this claim creates an alternative source of jurisdiction for this court to review the termination. That is, if defendant terminates a contract for default, and demands return of progress payments because of that default, arguably this presents a case appropriately to be resolved by this court. The termination for default becomes an adjunct to the claim for return of progress payments, a monetary claim.

A. Demand for Unliquidated Progress Payments

Defendant argues that the Navy failed to include all elements of a final decision in its February 5, 1991 letter as set forth in the FAR, *48 C.F.R. § 33.211(a)(4) (1987)*. Thus, no final decision was issued and this court lacks jurisdiction over the

[1] The December requests for equitable adjustment were converted to claims under the CDA by plaintiffs' February 18, 1991 letter requesting a final decision. The parties had stopped negotiating plaintiffs' equitable adjustment requests and a dispute had arisen between the parties. *Dawco Constr., Inc. v. United States*, 930 F.2d 872, 878 (Fed. Cir. 1991) (dispute necessary for a request to be converted into a claim).

demand. *41 U.S.C. § 605 (1988).* In addition, the Government contends that the February letter did not rise to the level of a government claim because a dispute between the parties had not occurred. *Dawco Constr., Inc.*, 930 F.2d at 877; *Dynalec Corporation*, ASBCA No. 40860, 91-1 B.C.A. (CCH) P23,553 (1990) (citing *Crippen & Graen Corp. v. United States*, 18 Cl. Ct. 237 (1989)).

It was not necessary for the Navy's February correspondence to comply with all requirements of *48 C.F.R. § 33.211(a)(4) (1987)* to be considered a final decision. *Placeway Constr. Corp. v. United States*, 920 F.2d 903, 906-07 (Fed. Cir. 1990) (setoff considered a government claim without the boilerplate language usually associated with a decision). The February letter was a demand for the return of progress payments. After the letter was issued, plaintiffs informed the Navy that they disputed the demand. With the dispute present, the parties entered into the Deferment Agreement.

The Deferment Agreement contained recitals to the effect that the Contracting Officer had demanded payment of $ 1,352,459,644; that the contractors would appeal the "final decision" of the Contracting Officer to the Board or to this court; that the contractors had requested deferment of collection action by the Government "regarding the amount demanded by the Contracting Officer"; that the contractors were jointly and severably liable for the amount demanded; and that collection of the government's claim would be deferred.

Thereupon, the contractors acknowledged the government's demand in the amount of $ 1,352,459,644; they "disagreed that any amount is due to the Government"; they agreed to pay interest in the amount demanded; and they reserved the right to "pay to the Government all or any of the amount determined to be due by the Contracting Officer's decision."

In return, the Government agreed to take no action "to enforce collection of the amount demanded" pending action by the court; and reserved the right to require immediate payment of $ 1,352,459,644 should plaintiffs fail to "file suit in the Claims Court on the Contracting Officer's final decision. . . ."

The Deferment Agreement constituted a final decision under the facts of this case. It contained the necessary elements of a final decision and exhausted plaintiffs' administrative remedies. *See Placeway*, 920 F.2d at 906-07. Nothing in the Deferment Agreement suggests that the parties intended to negotiate further, or even to discuss the amounts demanded.

B. The Default Termination

Defendant argues that we lack jurisdiction to decide the default termination, a non-monetary claim, unless it is tied and subordinate to a money claim. *Austin v. United States*, 206 Ct. Cl. 719, 723 (1975). Because neither plaintiffs' claims nor the

government's claim for return of progress payments meets this criterion, the court lacks jurisdiction. *Id.* at 723.

Austin involved a Navy enlisted man's petition to the court for correction of his military records and for award of back pay. *Austin*, 206 Ct. Cl. at 721. The *Austin* case interpreted one of our jurisdictional statutes, *28 U.S.C. § 1491(a)(2) (1988)*:

> To provide an entire remedy and to complete the relief afforded by the judgment, the court may, as an incident of and collateral to any such judgment, issue orders directing restoration to office or position, placement in appropriate duty or retirement status, and correction of applicable records, and such orders may be issued to any appropriate official of the United States.

The Court of Claims noted that the affirmative relief mentioned in the first sentence "can be given only where a money judgment is entered; that is the 'judgment' of which the statute speaks." *Id.* at 723. We agree. However, this is not a military pay case, as was *Austin* and the cases relied upon by the *Austin* court.

The court's reference to a declaratory judgment being "tied and subordinate to" a money claim is not applicable to this government contract case in light of the recent decision in *Overall Roofing & Constr.*,

Inc. v. United States, 929 F.2d 687 (Fed. Cir. 1991). The issue in *Overall Roofing* was "whether the Claims Court has jurisdiction over a case contesting only the propriety of a termination for default and presenting no claim for money; in other words, one asking only for a declaratory judgment that the termination was wrongful." *Overall Roofing*, 929 F.2d at 687-8. This was the only issue in *Overall*, and the answer was No.

In comparing the court to the Boards of Contract Appeals, the Federal Circuit noted, "In light of the greater formality of the Claims Court . . . the more efficient approach is to appeal all issues together." *Overall Roofing*, 929 F.2d at 690. It did not say the issues should be tied, or even associated. This indicates to us that a money claim must be presented with the termination claim at the time the complaint is filed.

The legislative history of *28 U.S.C. § 1491(a)(2) (1988)* shows that Congress wanted this court to hear all aspects of a case together, just as the Federal Circuit ruled in Overall Roofing. The first part of *§ 1491(a)(2)* addresses civilian and military pay cases. "In those cases, the Court of Claims can grant a monetary judgment but cannot alter the serviceman's military status. This bill would permit the Court of Claims to grant such military personnel relief collateral to and consistent with the judgment. . . . When the Court of Claims does have jurisdiction over any case before it, this bill will enable the court to grant all necessary relief *in one action*." (emphasis

supplied). H.R. Rep., No. 92-1023, 92d Cong., 2d Sess. 3 (1972).

The House Report concludes as follows: "It is the opinion of this committee that the aim of modern practice [is] to avoid repetitive lawsuits and to make it possible to dispose of all the claims and to adjudicate all of the rights of the parties in a single proceeding. . . . The committee has concluded that [this amendment] would improve the administration of justice in the Court of Claims by simplifying the procedure and reducing the costs incurred in litigation and in the pursuit of administrative remedies." *Id.* at 4.

The stated aim of Congress, as well as that of the Federal Circuit in *Overall Roofing*, was to encourage this court to resolve related issues in one proceeding. This case is one which Congress and the Federal Circuit direct us to "appeal all issues together." *Overall Roofing*, 929 F.2d at 690.

If *Overall Roofing* could be construed to require some type of relationship between the termination and a monetary claim, plaintiffs' claims and defendant's demand for the return of unliquidated progress payments would satisfy this condition. The reasons for defendant's termination for default are intertwined with the reasons for which plaintiffs seek the additional money in the December requests. Defendant's demand for return of progress payments was an integral part of the termination for default.

The Claims Court has held the government's demand for return of progress payments to be the monetary aspect of the termination for default. *Sharman Co. v. United States*, No. 90-108C (Cl. Ct. Dec. 20, 1991). When a contract is terminated for default, "the boundaries of a Government claim, as defined by procurement regulations, have been marked out. The issuance thereafter of a contracting officer's demand for return of unliquidated progress payments is simply a quantification of the Government's claim rather than the assertion of a new or different demand." *Sharman*, slip op. at 6. The court found that the amount of the government's claim was not in dispute; rather, the government's right to assert default was the issue. In that circumstance, the "final decision" was surplusage. The government's demand for return of progress payments was itself the monetary aspect of the termination for default. *Id.*, at 6.

We do not reach the *Sharman* issues because the Deferment Agreement was tantamount to a final decision under the facts of this case. Furthermore, the requirements of Overall Roofing are met by the monetary claims.

CONCLUSION

We reviewed classified documents referred to in the record to determine the intent of the parties to this contract. The substance of these documents is not included so that the Opinion itself would not be classified. However, the documents are compatible

with this Opinion, particularly as it relates to defendant's arguments concerning privity.

The court takes this opportunity to urge the parties once again to settle this case. Common sense suggests that it should not be tried, and settlement should occur early in the process rather than later. Recently, defendant has shown a willingness to consider settlement in the public interest. We encourage this approach.

The court will agree to a reasonable time for the parties to discuss settlement at the appropriate levels; we have offered offices to facilitate such discussions. However, the parties are advised that this case will proceed in accordance with normal practice in absence of settlement. Counsel will submit proposed trial dates and reasonable deadlines for discovery. The court will issue a schedule for summary judgment motions on Count II of the complaint. Summary judgment motions on other Counts may not be filed at this time, unless they are closely related to the merits of Count II.

1. Defendant's motion to dismiss is DENIED in part.

2. On or before March 23, 1992, plaintiffs will brief defendant's assertion that we lack jurisdiction to hear post-complaint claims. Defendant may respond on or before April 10, 1992.

3. The court will entertain a motion to remove "McDonnell Douglas/General Dynamics Team" as plaintiff.

SO ORDERED.

ROBERT H. HODGES, JR., Judge

/s/ Robert H. Hodges. Jr.
Robert H. Hodges, Jr.
Judge

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91-1204C

IN THE UNITED STATES CLAIMS COURT

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,

Plaintiffs,

v.

THE UNITED STATES,

Defendant.

DEFENDANT'S MOTION TO DISMISS PLAINTIFFS' CLAIMS RELATED TO "SUPERIOR KNOWLEDGE" IN ALLEGED OTHER LOW OBSERVABLE WEAPONS PROGRAMS

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APRIL 1, 1992

* * * *

SUMMARY OF ARGUMENT

Plaintiffs' "superior knowledge" argument must fail. As a matter of law, plaintiffs may not impose a sweeping duty to disclose in this case because the A-12 program and the alleged other special access programs to which plaintiffs claim a right of access were separate, compartmentalized programs. Moreover, the Government simply cannot be held to an **implied** duty to disclose military secrets. Acceptance of plaintiffs' argument would grossly distort the "superior knowledge" doctrine **and** seriously undermine the United States' control over the Nation's military secrets.

* * * *

IN THE UNITED STATES CLAIMS COURT

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DECLARATION OF PETER C. EAMES

I, Peter C. Eames, declare:

1. I am the Deputy Security Director in the Office of the Assistant Secretary of the Air Force for Acquisition.

2. As such, I am familiar with and charged with enforcing the standards and procedures governing the protection, use, processing, transportation, destruction, and disclosure of information pertaining to highly restricted and classified programs. I have held this and similar substantive policy making positions in Air Force Special Access Programs for 14 years. My responsibilities include recommending security policies and classifications of information classified and protected within special access programs. I have had responsibility for the B-2 and F-117A programs from the first day of the programs' inceptions.

3. Classification of information within the Department of Defense is done in accordance with Executive Order ("E.O.") 12356, which prescribes a uniform system for classifying, declassifying, and safeguarding national security information. Executive Order 12356 (April 2, 1982), 3 C.F.R. 166 (1983), *reprinted in* 50 U.S.C.A., at 208 (1991); and Presidential Order of May 7, 1982, 3 C.F.R. 257 (1983), *reprinted in* 50 U.S.C.A., at 217 (1991). E.O. 12356 authorizes three levels of classified information: top secret, secret, and confidential.

4. Pursuant to Department of Defense ("DOD") Directive 5200.1, originally issued in 1982, it was (and is) the policy of the Department of Defense to use traditional classification categories wherever possible. An agency head (in this case the Secretary of the Air Force, with the concurrence of the Deputy Secretary of Defense) may designate a program as a "special access program" (discussed below) when he determines that the information is of such sensitivity and importance that the normal security procedures authorized for a secret or top secret program are not sufficient to limit access appropriately. DOD Directive 5200.1, § 159.120, 47 Fed. Reg. 38,284, 38,316 (1982) (codified as revised at 32 C.F.R. § 159a.80 (1991)).

5. When necessary, such additional protection for classified information is available to programs designated as "special access programs." *See* 32 C.F.R. § 2001.45 (1987) (criteria for special access program status). Special access program status is intended to protect those specially sensitive

programs that cannot be adequately protected by the level of security and access controls afforded secret or top secret non-special access programs. See 32 C.F.R. § 2001.45. The "special access" designation is reserved for particularly sensitive classified programs in order to control the access, distribution, and protection of information pertaining to these special access programs.

6. An individual must possess a security clearance of secret or top secret as a prerequisite for access to a special access program. Possession of a security clearance is only the first step toward approval for access to a special access program. These programs are characterized in part by an additional adjudication, to a more stringent standard than the adjudication for a security clearance. *See* DOD Directive 5200.2-R, 52 Fed. Reg. 11,219 (1987) (codified at 32 C.F.R. § 154) (outlining security reviews of personnel in special access programs).

7. Special access programs also impose "need to know" and access controls beyond those normally required by DOD regulations for access to confidential, secret, and top secret information. Access to information within a special access program is granted only to those persons who are essential to the successful completion of the program, and who meet all stipulated security requirements. Other more stringent security measures in effect in special access programs are enhanced physical, technical, communications, computer, operations, and information security.

8. Special access programs may be acknowledged (overt) or unacknowledged (covert) in nature. The mere existence of an unacknowledged program is classified within the boundaries of the special access program. That is, one must be approved for access before one may know that the program exists at all.

9. A further aspect of special access programs is that they are "compartmented." See section 4.2 of E.O. 12356. That is, the information in the program is, in effect, walled off from other classified information and programs. For example, it is not uncommon that individuals, either Government or contractor personnel, may work in a secure facility that contains more than one special access program. An individual may have access to one special access program while his colleagues have access to different special access programs. Despite the fact that the individuals are professional colleagues, that they possess the requisite security clearances, and they work in the same secure facility, such individuals are still prohibited, absent being given access to another program, to share special access information across program boundaries. The purpose of this requirement is that in the event of a breach of security the potential damage is limited to that one special access program. In effect, the "compartmented" nature of special access program works as a damage control brake in the event of an unauthorized disclosure.

10. I am familiar with the F-117A and B-2 aircraft programs. The Department of the Air Force

has oversight responsibility for both programs. The F-117A is a "stealth," or low-observable, fighter plane. The B-2 is a stealth long-range bomber.

11. Both the F-117A and the B-2 aircraft programs are classified, special access programs, and have been from their inception. Both were, therefore, classified, special access programs during the period 1986 through 1988. Additionally, the B-2 program was created and operated as unacknowledged programs until 1980. The F-117A was also created and operated for a period of time as an unacknowledged program. After that time, and to the present, these programs have continued as acknowledged special access programs.

12. In 1980, the Secretary of Defense announced that the United States was building a "stealth bomber" and conducting flight tests. In 1983, the award of the contract to build the B-2 was announced. No further information was released. In April 1988, an artist's conception of the bomber was released. On November 22, 1988 slightly more information was released upon roll-out of the B-2 bomber. All these releases were conducted under strictly controlled conditions to assure that only a small amount of information was released. All other information about the B-2 remained classified.

13. The F-117A program was officially acknowledged by DOD in November 1988. At that time DOD released a general statement about the nature and scope of the program. All other information about the program retained its classification.

14. Only those persons with the requisite need to know, and background review, were granted access to the B-2 or F-117A programs. National security reasons for these special precautions are discussed below.

15. I have reviewed plaintiffs' Sixth Set of Interrogatories and plaintiffs' Eighth Set of Requests for Production of Documents in this case.

16. Plaintiffs' document requests 351-356 seek specific information from the F-117A and B-2 programs. In document requests 351 and 354, plaintiffs seek all specifications and all operational requirements for low observability for the B-2 and F-117A aircraft, respectively. In requests 352 and 355, plaintiffs seek a broad array of contractual documents from the two programs, including information relating to the tooling and manufacturing of low observable parts. Finally, in requests 353 and 356, plaintiffs seek all of the development schedules, including modifications, for the B-2 and F-117A programs, respectively.

17. To the extent that plaintiffs' discovery requests seek information from the F-117A or B-2 programs, up through 1988 access to any such information was barred except to those who had been granted access to the F-117A or B-2 programs, respectively. Plaintiffs' document requests 351 through 356 each call for information that was up through 1988 classified, special access information.

18. The unauthorized disclosure of the information reasonably could be expected to cause grave damage to the national security. The United

States is the world leader in the production and operation of low-observable technology aircraft. Air Force pilots have flown our F-117A stealth fighters in combat, without any U.S. loss of life or aircraft. We believe that no foreign country presently has either the capability to build low observable aircraft or the capability to develop a credible countermeasure to this technology. The United States has very limited capability to counter this technology, should it be developed and used against us by a foreign country. The B-2 aircraft is a newer generation of stealth technology and thus contains even more sensitive and advanced technology than the F-117A.

19. If the stealth technology from classified, special access programs, such as the B-2 or F-117 is disclosed without authorization, this will weaken our country's ability to defend itself and could place at risk our aircraft and the lives of the crews of those aircraft.

Pursuant to section 1746 of title 28, United States Code, I hereby declare under penalty of perjury that the foregoing is true and correct.

/s/ PETER C. EAMES
PETER C. EAMES
Deputy Security Director
Assistant Secretary
of the Air Force (Acquisition)

Executed this 8th day of September, 1992.

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDonnell Douglas Corporation and General Dynamics Corporation	)	
Plaintiffs,	)	No. 91-1204C
v.	)	(Judge Hodges)
The United States,	)	
Defendant.	)	

DECLARATION OF SECRETARY OF THE AIR FORCE DONALD B. RICE

I, Donald B. Rice, declare:

1. I am the Secretary of the Air Force. As such, I am the head of the Department of the Air Force. I am responsible for and have the authority necessary to conduct all affairs of the Department of the Air Force. Subject to the authority, direction and control of the Secretary of Defense, I am also responsible for the formulation of policies and programs by the Department of the Air Force that are fully consistent with national security objectives and policies established by the President and the Secretary of Defense.

2. The purpose of this declaration is to provide the rules the Air Force has instituted with respect to national security information contained in the B-2 "Advanced Technology Bomber" and F-117A "Stealth Fighter" aircraft programs. The statements

in this declaration are based upon my personal review and consideration of the matter.

3. The documents which are the subject of the Court's order of October 30, 1992, contain important national security information. Executive Order ("E.O.") 12356 prescribes a uniform system for classifying, declassifying and safeguarding national security information. E.O. 12356 authorizes three levels of classified information: Top Secret, Secret, and Confidential. Different portions of the information sought in the Requests for Production have been classified as "confidential" "secret" and "top secret" under Executive Order 12356. Disclosure of information classified as "confidential" reasonably could be expected to cause damage to the national security. Disclosure of information classified as "secret" could reasonably be expected to cause serious damage to the national security. Disclosure of information classified as "top secret" could reasonably be expected to cause extremely grave damage to the national security.

4. In addition, I have designated portions of the B-2 and F-117A programs as "Special Access Programs" under E.O. 12356. The "Special Access" designation is reserved for particularly sensitive classified programs in order to further control the access, distribution, and protection of information pertaining to it. Special Access Programs impose "need-to-know" and access controls beyond those normally required by Department of Defense regulations for access to Confidential, Secret, or Top Secret information. Access to information within a

Special Access Program will be granted only to those persons who are essential to the successful completion of the program, or who are required for proper coordination and oversight, and who meet all stipulated personnel security requirements. Thus, in addition to being classified "confidential" "secret" and "top secret", the information at issue is further classified as "Special Access Required."

5. To comply with the Executive Order 12356 requirement to limit access to the greatest extent possible, I have determined the following: a) not more than 10 individuals (including counsel, consultants, or engineers) representing the plaintiffs, are hereby authorized access to the Secret/Special Access level of the B-2 and F-117A programs; b) not more than 4 of those 10 individuals are hereby authorized access to the Top Secret/Special Access level of the B-2 and F-117A programs. Each individual must meet all clearance eligibility criteria in the programs' security guides.

6. The Air Force will provide plaintiffs access to the material identified in plaintiffs' revised Requests for Production 351 through 355, dated October 21, 1992. The material is located and available for review at Wright-Patterson Air Force Base, Ohio, and at Sacramento Air Logistics Center in California.

7. Minimum security rules and procedures required to competently protect Air Force Special Access Required information are contained in the

Program Security Guides for the B-2 and F-117A aircraft programs.

8. The unauthorized disclosure of the national security information at issue reasonably could be expected to cause extremely grave damage to the national security. The United States is the world leader in the production and operation of low-observable technology aircraft. Air Force pilots have flown our F-117A stealth fighters in combat, without any U.S. loss of life or aircraft. We believe that no foreign country has either the capability to build low observable aircraft or the capability to develop a credible countermeasure to this technology. The United States has very limited capability to counter this technology, should it be developed and used against us by a foreign country. The B-2 is a newer generation of stealth technology and thus contains even more sensitive and advanced technology than the F-117A. If the stealth technology from classified, special access programs, such as the B-2 or F-117A is disclosed without authorization, this will weaken our country's ability to defend itself and could place at risk our aircraft and the lives of the crews of those aircraft.

9. It is my judgment, after personal consideration of the matter, that the national security information at issue in this litigation. and described herein, must be limited and strictly controlled in the interests of the national security of the United States. The limited access authorized in paragraph 5 above is consistent with the strict limitations that are applied to government

employees for access to this national security information.

Pursuant to Title 28, Section 1746, I hereby declare under penalty of perjury that the foregoing is true and correct.

/s/ DONALD B. RICE
DONALD B. RICE
Secretary of the Air Force

Executed this 20th day of Nov. 1992.

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

No. 91-1204C

(Filed: November 23, 1992)

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	28 U.S.C. § 1292(d)(2) Standards for Certification for Interlocutory Appeal
v.	)	
UNITED STATES OF AMERICA,	)	
Defendant.	)	

Francis M. Gaffney, Sonnenschein, Nath & Rosenthal, St. Louis, Missouri, for plaintiff McDonnell Douglas Corporation; John W. Walbran, General Counsel, St. Louis, Missouri, of counsel; Herbert L. Fenster, McKenna & Cuneo, Washington, D.C, for plaintiff General Dynamics Corporation; Robert H. Duesenberg, General Counsel, Falls Church, Virginia, of counsel.

Mary Mitchelson and Bryant G. Snee, United States Department of Justice, Washington, D.C., for

defendant; Stephen R. O'Neill, Department of the Navy, Washington, D.C., of counsel.

ORDER AND OPINION

BACKGROUND

Defendant filed a motion in April 1992 to dismiss plaintiffs' counts based on alleged government superior knowledge. Because the A-12 and other special access programs were separate and compartmented programs, defendant argued that as a matter of law plaintiffs could not impose a duty to disclose such information. Plaintiffs responded that no classified information exception to the superior knowledge doctrine exists.

Both parties relied on *J.A. Jones Construction Company v. United States*, 390 F.2d 886 (Ct. Cl. 1968). Defendant interpreted *J. A. Jones* to mean that the Government does not have a duty to disclose superior knowledge if the disclosure would threaten national security. Plaintiffs argued that the Government is not free to mislead a contractor by silence solely because the superior knowledge is classified.

After oral argument in June, we ruled from the bench that plaintiffs' superior knowledge counts could not be stricken from the complaint at that stage. In essence, we ruled that *J.A. Jones* opened the door to very limited discovery, and asked the parties to craft a reasonable discovery process that would allow plaintiffs to obtain the information they

needed to prove their case without disclosing details of the Government's superior knowledge.

Subsequently, defendant sought interlocutory appeal of that ruling to the Federal Circuit. Defendant asked to be heard on its motion for certification, and we held oral argument on November 5. At that hearing, defendant argued that the court's June decision meets the applicable standards for certification. These standards require (1) a controlling question of law with respect to which there is a substantial ground for difference of opinion, and (2) that an immediate appeal may materially advance the ultimate determination of litigation. 28 U.S.C § 1292(d)(2) (1988).

The record containing the June decision denying defendant's motion to dismiss is classified, and we have not issued reasons for that decision in a non-classified form.

Therefore, we take this occasion to address the June ruling in a limited way. Whether an appeal would materially advance termination of the litigation is not discussed here because both standards must be met, and we find that "a substantial ground for difference of opinion" does not exist.

DECISION

A "substantial ground for difference of opinion" requires an absence of controlling judicial authority on an issue. At this stage of the proceedings, we are

not persuaded that the law is so unclear. Because of the presumptions enjoyed by a party defending a motion to dismiss on the pleadings, defendant must show as a matter of law that it could never have a duty to disclose superior knowledge if that knowledge were classified. We believe that certification of such an issue would be inappropriate at this time.

Helene Curtis Industries, Inc. v. United States, 312 F.2d 774 (Ct. Cl. 1963), established a four-part test for a superior knowledge claim, paraphrased here as follows: (a) defendant knew about the special information, (b) plaintiff neither knew nor had reason to know the information, (c) defendant failed to supply the information, and (d) this failure misled plaintiff.

These portions of the *Helene Curtis* holding apply to our case:

1. "Government permitted plaintiff . . . to enter a bid for this novel product and undertake a process . . . which was undoubtedly planned without the significant information . . . possessed by defendant." 312 F.2d at 777.

2. "[T]he fixed price contractor of course bears the burden of unanticipated increases in costs . . . . [A]n end-product specification normally leaves it to the contractor to perform as best he can . . . , but that does not excuse the defendant from liability if it breaches an independent duty to reveal data . . . ." 312 F.2d at 777-78 (citations omitted).

3. "There are many contracts . . . where a contractor can reasonably be expected to seek the facts for himself . . . . The Government may be under no duty to volunteer information in its files. But . . . there are other instances in which the defendant is clearly under such an affirmative obligation and cannot remain silent." 312 F.2d at 778 (citations omitted).

4. "Government, possessing vital information which it was aware the bidders needed but would not have, could not properly let them flounder on their own." 312 F.2d at 778.

The Navy sought a "novel product" in the A-12, a Stealth fighter which could land on an aircraft carrier. The Government argues as it did in *Helene Curtis* that this was a full scale development contract - an "end-product" for which the Government "contracted for technical know-how and manufacturing skills . . . ." 312 F.2d at 777. But plaintiffs have evidence that defendant anticipated sharing earlier Stealth technology with its contractors. Defendant may have possessed vital information which it could have known would assist plaintiffs, and plaintiffs allege that defendant remained silent. Thus, plaintiffs have alleged a cause of action that is supported by existing law.

J.A. Jones cites "the *established rule* that, while the defendant had no obligation to prevent . . . the avalanche that buried the contractor, it was not free, if it was aware of the impending avalanche and knew that J.A. Jones was not, to stand aside and let the

bidder be overwhelmed without a warning." *J.A. Jones*, 390 F.2d at 888 (emphasis added).

Though classified information was involved in *J.A. Jones*, the court focused on the issue of imputed knowledge among government agencies: "If the Air Force were the formal contracting agency [instead of the Army Corps of Engineers], there would be no doubt, on these facts, that defendant would be liable . . . ." 390 F.2d at 890. The court ultimately held the Government liable under the standards of *Helene Curtis* for the Air Force's failure to disclose its knowledge.

A key ruling of *J A. Jones* for our purposes is found at page 893, note 14: "While some aspects of the Air Force's plans undoubtedly were classified, the evidence falls far short of proving that a general warning to plaintiff would have rent the security blanket."

Though details of the classified information may not have been crucial; a warning may have been sufficient. In any event, the court clearly ruled that the Government had a duty to make *some* disclosure based upon its superior knowledge even though the basis for that knowledge was classified.

Defendant has argued repeatedly that Stealth technology includes some of the Government's most precious secrets. Defendant has produced affidavits to that effect, and we have no doubt of it. Defendant argues that the United States must not be required to share its most highly classified technology with

plaintiffs. However, we do not view this as a natural result of the court's refusal to dismiss the superior knowledge counts.

Plaintiffs allege in essence that defendant allowed them to go astray; that defendant knew of the impending avalanche and did nothing. A warning may have been enough to satisfy requirements of the superior knowledge doctrine. Arguably, extensive sharing of sensitive technology would not have been necessary -- it may not be necessary now. We have held only that plaintiffs were entitled to prove that defendant knew of the avalanche and did nothing about it.

CONCLUSION

Helene Curtis and *J.A. Jones* direct that plaintiffs' superior knowledge counts should not be dismissed at the pleadings stage. Because this is clear authority from the Court of Appeals for the Federal Circuit, we cannot certify that a substantial ground for difference of opinion on this issue exists. Defendant's motion is therefore DENIED; the Order filed October 30 remains in effect.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

Nos. 09-1298 & 09-1302

Supreme Court, U.S.
NOV 12 2010
OFFICE OF THE CLERK

IN THE
Supreme Court of the United States

GENERAL DYNAMICS CORPORATION,
Petitioner,
v.
UNITED STATES OF AMERICA,
Respondent.

THE BOEING COMPANY,
Petitioner,
v.
UNITED STATES OF AMERICA,
Respondent.

On Writ Of Certiorari To The
United States Court Of Appeals
For The Federal Circuit

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IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

SECOND AMENDED UNCLASSIFIED COMPLAINT

Plaintiffs McDonnell Douglas Corporation and General Dynamics Corporation, pursuant to RCFC 15(a), hereby amend their complaint by leave of Court. For their Second Amended Unclassified Complaint, Plaintiffs allege as follows:

The Parties

1. Plaintiff, McDonnell Douglas Corporation ("MDC"), is a corporation organized under the laws of the State of Maryland, with its principal place of business in St. Louis, Missouri.

2. Plaintiff, General Dynamics Corporation ("General Dynamics"), is a corporation organized under the laws of the State of Delaware,

with its principal place of business in St. Louis, Missouri.

3. MDC through its McDonnell Aircraft Company Division, located in St. Louis, Missouri, and General Dynamics through its Fort Worth Division, located in Fort Worth, Texas, were each a party to the Contract with the United States at issue in this action. (For the purpose of this Complaint, the companies are referred to as the "Contractors.")

4. Defendant is the United States Government, which was a party to the Contract at issue, acting by and through the Naval Air Systems Command ("NAVAIR" or "Navy").

Jurisdiction

5. On January 13, 1988, the Navy awarded Contract No. N00019-88-C-0050 (the "A-12 FSED Contract" or "Contract") to the Contractors for the full scale engineering development ("FSED"), with options for initial production quantities, of the Advanced Tactical Aircraft ("ATA"). The ATA was later designated the "A-12."

6. On December 31, 1990, the Contractors submitted written, certified claims to the contracting officer seeking equitable adjustments in price and schedule under the Contract, in the amount of a $1,401,181,205 increase to the target price. The Contractors also alleged alternatively breach of contract by the Navy; and that the Contract was void or voidable, such that the Contractors were entitled to compensation under an implied-in-fact contract.

7. On January 7, 1991 the Navy's contracting officer issued a final decision which purported to terminate the Contract for default, and which constituted a *de facto* denial of the Contractors' claims. (Exhibit A.)

8. Based on the final decision alleged in paragraph 7 above, on February 5, 1991, the Navy issued a formal demand under Federal Acquisition Regulation ("FAR") § 32.610 (48 C.F.R. § 32.610 (1990)), which itself constituted a government claim, for the return of unliquidated progress payments made to the Contractors during performance of the A-12 FSED Contract, in the amount of $1,352,459,644. The demand stated that any portion of that amount not paid to the government "shall be subject to interest."

9. On June 7, 1991, the Contractors submitted revisions and updated pricing on most of the claims previously submitted on December 31, 1990. The Contractors requested an equitable adjustment in price and schedule under the Contract in the amount of a $1,033,197,644 increase to the target price for the updated claim elements.

10. On June 26, 1991, the Contractors submitted to the Contracting Officer the "A-12 Termination Settlement Proposal and Claim" in the amount of $1,286,127,692 with respect to full-scale development and the first two production options. The certified claim challenged the validity of the termination of the Contract for default and the monetary recovery sought was based on the Contract

provisions and regulations applicable to terminations for convenience.

11. On July 26, 1991, the Contractors submitted a revised and updated claim entitled "Claim for Payment of All Incurred Performance Costs Based on Invalidity of Fixed-Price Contract," which had been originally submitted on December 31, 1990.

12. On July 26, 1991, the Contractors submitted a claim entitled "Claim for Improper Withholding of Progress Payments." The monetary amount sought for this Claim was included within the amount claimed in the "A-12 Termination Settlement Proposal and Claim."

13. The claims described in paragraphs 6 and 9-12 were certified, for purposes of the Contract Disputes Act, by the General Dynamics senior company official in charge at General Dynamics' Fort Worth Division, and by the MDC senior company official in charge at MDC's McDonnell Aircraft Company division. Additional certificates by both officials were also provided in the form suggested by the Navy for the claims described in paragraphs 9-12.

14. By letter dated August 5, 1991, the contracting officer stated that because this suit was pending, he would not take any action regarding any of the claims described in paragraphs 6 and 9-12 without Court direction. The contracting officer's expressed intention not to issue a decision constitutes denial of the claims set forth in paragraphs 6 and 9-12. 41 U.S.C. § 605(c)(5).

15. The suit seeks *de novo* review of the contracting officer's final decision on each of the claims referred to in paragraphs 6-12. This Court has jurisdiction over this action pursuant to section 10(a) of the Contract Disputes Act of 1978 (41 U.S.C. § 609(a) and 28 U.S.C. § 1491(a)(2) (1988)).

Major Weapon System Acquisition Requirements

16. Department of Defense directives established a structured progression of phases for major weapon systems such as the A-12.

17. The Department of Defense required that the A-12 program include a concept formulation phase, a demonstration and validation phase, and a full scale development phase. Prior to advancement to the next phase, the Navy was required to conduct a detailed program review including: (1) assessment of program status; (2) identification of risk areas and assessment of the degree of risk reduction; (3) assessment of commonality with previous solutions under other weapon systems programs; (4) analysis of test results; and (5) assessment of procurement strategy in light of program cost and risk assessments. Programs were not permitted to proceed into the next phase without a favorable recommendation based on such a detailed review as required by Department of Defense Directives 5000.1 dated September 1, 1987 and 5000.2 dated September 1, 1987.

18. The Department of Defense required that A-12 program officials consider all potential solutions to A-12 requirements that were available

from other defense programs, before and during FSED. Department of Defense Directive 5000.1 dated September 1, 1987, ¶ D.6.

19. Department of Defense Directive 5000.1 also states that: "Contract type shall be consistent with all program characteristics including risk. Fixed-price contracts are normally not appropriate for research and development phases. For such efforts, a cost reimbursable contract is preferable because it permits an equitable and sensible allocation of program risk between the contracting parties." *Id.*, ¶ 9.g.

20. The Navy required that "over-specification" and unnecessary requirements be eliminated from the A-12 solicitation and the A-12 Contract. SECNAV Instruction 4210.6 dated November 20, 1985, ¶¶ 4. b, 6. a.

21. The Navy also required that A-12 program officials establish and maximize communications within the Navy, with the Office of the Secretary of Defense, and with the other military services, including the United States Air Force, to eliminate redundancy and duplication and to increase commonality. *Id.*, ¶ 6.a.

22. The Navy required that program managers, including the A-12 program manager, structure the program to be consistent with the foregoing requirements, and to revise program structure as necessary to comply with the requirements, from program inception through completion. *Id.*, ¶ 6.b.

23. Prior to commencement of FSED for the A-12, the Navy required certification that the A-12 development specifications had been reviewed and tailored to include only those items necessary to meet operational requirements. The Navy also required certification that the proposed A-12 development was planned so as to achieve maximum practical commonality. *Id.*, ¶ 6.d.

A-12 Program Inception

24. In February 1984, the Department of Defense initiated the ATA program to develop a carrier-based, medium attack aircraft integrating state-of-the-art, low observable technologies with other advanced aircraft technologies.

25. At the time the A-12 Program was initiated, it was subjected by the Navy to unusually strict security controls. The substance and even existence of the A-12 Program were highly classified. The existence of the program was later officially revealed, but at all times the Navy maintained the A-12 Program in a classified, special access status in which information concerning the A-12 was tightly controlled for national security purposes.

26. By letter dated October 2, 1984, the Navy requested MDC, General Dynamics, Lockheed Corporation and Northrop Corporation to form "teams" of two or more companies among themselves or with other companies to compete for the ATA program.

27. The Navy limited the potential competition to those companies that had the required

"team" arrangements. The Navy intended the "teaming" concept to provide it with two sources for later production contracts for the A-12.

28. On November 2, 1984, MDC and General Dynamics entered into a "Teaming Agreement" for the purpose of competing for concept formulation studies, full-scale development and production of the ATA.

29. The Teaming Agreement set forth the terms and conditions governing MDC's and General Dynamics' respective performance under any ATA contracts. By its terms, the Teaming Agreement did not create a joint venture or partnership between MDC and General Dynamics.

30. On November 28, 1984, the Navy awarded fixed-price contracts: one to General Dynamics and MDC and another to a team formed by Northrop with two other companies.

31. The contracts provided for performance of twelve-month studies for the Concept Formulation Phase of the ATA program.

32. In November 1985, General Dynamics and MDC submitted a Concept Formulation Phase report that set forth alternative concepts for the aircraft and preliminary estimated costs for the demonstration and validation phase and FSED phase of the ATA program.

33. The Contractors' Concept Formulation Phase report proposed a lengthy demonstration and validation period during which eighteen technologies, and the integration of those

technologies, would be studied to reduce development risks prior to entry into FSED.

34. In their report, the Contractors estimated the costs necessary to perform the demonstration and validation phase at approximately $360 million (FY 1985 dollars) and FSED at $6.3 billion or greater (FY 1985 dollars).

35. In late 1985, the Navy adopted an "ATA Acquisition Strategy" that included an FSED funding ceiling of $4.2 billion (in FY 1985 dollars), mandated the use of a fixed-price type contract for FSED, and directed that the aircraft have an initial operational capability of no later than 1994.

36. The Navy's Acquisition Strategy also stated that the Navy and Air Force had been directed to form a joint committee to minimize "duplication" of development efforts on the Navy's ATA and the U.S. Air Force Advanced Tactical fighter, to engage in other cooperative efforts to reduce duplication of development activities, and to take advantage of previously-developed technologies.

37. On or about June 25, 1986, the Navy contracted for the demonstration and validation phase by formally modifying the Contractors' Concept Formulation Phase Contract to allow for limited demonstration and validation activities. The Navy's contract modification established a "not to exceed" price of $78 million for those activities. The Navy reduced the scope of the demonstration and validation phase to approximately 20 percent of that proposed by the Contractors.

38. The Navy directed the technical areas that would be investigated. In September 1986, in compliance with Navy direction, the Contractors submitted a revised proposal reflecting the substantial Navy-directed reductions in the scope of the effort to be accomplished during the demonstration and validation phase of the A-12 program, and the modification was definitized on that basis.

39. The funding and schedule restrictions imposed by the Navy on the demonstration and validation phase of the A-12 Program prevented the Contractors from performing studies that the Contractors later learned were essential to the reduction of the risks associated with development of the A-12, and to realistic estimation of development costs.

40. The Navy's funding and schedule limitations prevented reduction of program risks in the demonstration and validation phase, such that realistic estimation of development costs could not, in fact, be accomplished prior to the A-12 FSED Contract award.

41. Further, the compressed demonstration and validation schedule forced the Contractors to proceed into the FSED phase of the program on the basis of a proposal prepared from incomplete test data acquired during the demonstration and validation phase of the A-12 Program.

42. Technical, price and schedule risks, therefore, were not reduced sufficiently to permit lawful use of a fixed-price type contract for FSED.

43. On information and belief, the Navy was aware that these funding and schedule limitations unreasonably compressed the normal development cycle for a major weapons system such as the A-12, and prevented the Contractors from adequately reducing program risks and establishing an appropriate design approach prior to FSED Contract award.

44. The Navy's schedule compression and underfunding of the demonstration and validation phase of the A-12 Program, and the Navy's choice of a fixed-price type contract despite the existence of significant development risks, increased the Navy's obligation to share with the Contractors data within the government's possession that were vital to the Contractors' performance of the A-12 FSED Contract, to deal with the Contractors in good faith, and to cooperate and not to hinder the Contractors' performance.

45. Based on the available results of the demonstration and validation phase of the program, and the best information then available to the Contractors, the Contractors mistakenly believed that development risks had been reduced sufficiently to permit sensible risk allocation and realistic pricing of a fixed-price FSED Contract.

Related DOD Weapon System Development Programs

46. On information and belief, commencing in the late 1970's, the government sponsored the design, development and flight test of low observable

aircraft and other weapons systems through other classified, special access DOD programs.

47. These programs included, for example, the B-2 and F-117A aircraft.

48. On information and belief, most of these programs, and specifically the B-2 program, were conducted under cost-reimbursement type contracts.

49. On information and belief, those programs yielded information to the government that was vital to the Contractors' performance of their A-12 FSED obligations.

50. On information and belief, the vital information held by the government through the other classified, special access programs related to, among other things, weight estimation techniques, application of low observable technologies, propulsion system technologies, composite materials and composite manufacturing technologies, and avionics technologies (especially those relating to achievement of low observability).

51. Information generated within or about these programs was subject to extraordinary security and program access restrictions established and controlled by the government.

52. Prior to and at the time the A-12 FSED Contract was awarded, most of these programs were individually compartmented, "special access required" programs in which access to all information was classified and restricted to those who had been granted access upon special review of the individual's background and need-to-know.

53. In many cases, the very existence of the programs was classified and subject to strict "need-to-know" restrictions.

54. On information and belief, government organizations sponsoring these classified programs, including the Navy, established relationships between and among themselves providing for sharing of information on technical issues related to, and and on methods of designing, developing and manufacturing, such low observable aircraft and other weapon systems.

55. Prior to A-12 FSED Contract award, the Contractors requested access to various types of information held by or available to the Navy through other DOD classified programs.

56. The Navy failed to provide the Contractors with the requested information prior to, and, in most cases, subsequent to award of the A-12 FSED Contract.

57. As a result of the government's actions, vital information from these compartmented programs was unavailable to the Contractors during the demonstration and validation phase of the A-12 Program, during preparation of the Contractors' A-12 FSED proposals, and during performance of the A-12 FSED Contract.

58. On information and belief, timely access to vital information from these compartmented programs would have enabled the Contractors to achieve technical solutions without having to perform extensive and duplicative research and

development effort, and to alter their approaches in the demonstration and validation phase and in their proposals for the A-12 FSED Contract to reduce developmental risk and cost.

59. On information and belief, the government was aware that the withheld information was vital to the A-12 development, that the Contractors did not have available information from other, classified, special access programs, and had no means to obtain such information on their own.

60. Further, the government failed to inform the Contractors that a potential supplier's performance on a related ongoing radar subcontract for a Navy program was deficient. That information was not available to the Contractors. The A-12 radar specification was derived by the Navy from and closely paralleled the radar specification used in the other subcontract. Notwithstanding the Contractors' recommendations, the restrictive A-12 radar specification effectively limited the A-12 radar vendor competition by unfairly and unnecessarily favoring the radar vendor on the related subcontract for the other Navy program, resulting in selection of that vendor as the A-12 radar supplier.

61. The government also prevented the Contractors from discussing A-12 Program requirements with certain potential suppliers in order to permit realistic pricing of the Contractors' FSED and production proposals. For example, the Navy precluded the Contractors from discussing ejection seat requirements and pricing with the

Navy's sole source supplier, prior to award of the A-12 FSED Contract.

Request for Proposals for the A-12 FSED Contract

62. On December 19, 1986, only six months after contracting for the demonstration and validation phase, the Navy issued a Request for Proposals for the FSED phase of the ATA program.

63. The Navy required fixed-price type proposals for FSED with not-to-exceed prices for options for early production phases of the A-12 Program. Consistent with the Navy's ATA Acquisition Strategy, the RFP announced that only $4.2 billion (in FY 1985 dollars) would be available to the successful offeror for FSED and that the initial operational capability of the aircraft was to occur in 1994.

64. The Request for Proposals for the A-12 FSED Contract contained a comprehensive technical specification for the ATA. See Type Specification for Carrier-Based Advanced Tactical Aircraft Weapon System, TS-185 (5 December 1986) and associated Appendices A-G.

65. The Navy, having significantly reduced the scope of the demonstration and validation phase of the Program, and having failed to disclose knowledge within the government's exclusive possession or control from other classified programs that was vital to the Contractors' preparation of a realistic proposal and subsequent performance, warranted the adequacy of the specifications for the

purposes of development of the A-12 and of pricing the A-12 FSED Contract on a fixed-price basis.

66. On information and belief, the specifications were known by the Navy to be unattainable in several respects, exceeded the Navy's operational needs, and were intended by the Navy to be goals or objectives rather than firm requirements. To the extent the aircraft developed under the Contract failed to meet the specifications but still satisfied the Navy's operational needs, the Navy intended to revise the specifications and to accept the aircraft.

67. The Type Specification covered all significant performance requirements for the aircraft, including, inter alia, structural design criteria, propulsion system, avionics, and low observability requirements.

68. On information and belief, the Type Specification failed to reflect the government's knowledge of whether the specified levels of low observability and other performance requirements were achievable, or whether particular estimation, design and fabrication methods were suitable.

69. In response to the Navy's request, the Contractors submitted fixed-price type proposals for the A-12 FSED Contract and not-to-exceed prices for the related production options.

70. The Contractors submitted their initial technical proposal for FSED on March 6, 1987 (less than nine months after the Navy contracted for the demonstration and validation phase), the initial cost

proposal on March 30, 1987, a "Best and Final Offer" on September 15, 1987, and a second "Best and Final Offer" on October 26, 1987.

71. Based on the government's implied warranty of the specifications, the available results of the demonstration and validation phase of the program, and the best information then available to the Contractors, the Contractors believed prior to Contract award that development risks had been reduced sufficiently to permit sensible risk allocation and realistic pricing of a fixed-price type FSED Contract.

72. The Contractors' FSED and Production Option proposals were reasonable, given the development tasks as understood by them at the time the proposals were submitted.

73. The Contractors prepared their design for the A-12 based on the best information then available to them, including information from unclassified sources throughout the aerospace industry generally, and within the constraints of the performance and design requirements contained in the Navy's specification:

a. The Contractors estimated the weight of the A-12 aircraft based on the best information then available to them, including information from unclassified sources throughout the aerospace industry generally.

b. The Contractors designed the A-12 propulsion system, including inlets, engines and exhausts, based on the best information then

available to them, including information from unclassified sources throughout the aerospace industry generally.

c. The Contractors designed the A-12 avionics suite, including aircraft antennas, based on the best information then available to them, including information from unclassified sources throughout the aerospace industry generally.

d. The Contractors prepared their proposal for designing and manufacturing composite structures based on the best information then available to them, including information from unclassified sources throughout the aerospace industry generally.

74. On information and belief, prior to contract award senior Department of Defense officials advised against using a fixed-price form of contract for the A-12 FSED because, inter alia, technical, schedule and price risks had not been reduced adequately as required by law, regulation and Department of Defense policy and directives.

Award of the A-12 FSED Contract

75. On January 13, 1988, the Navy awarded the A-12 FSED Contract to the Contractors, as a fixed-price incentive contract with a ceiling price of $4,777,330,294, and a target price of $4,379,219,436.

76. On information and belief, the government knew at the time of the A-12 FSED Contract award that the concept formulation and demonstration and validation phases of the A-12

program had been insufficient to reduce developmental risks to a level at which realistic pricing or sensible risk allocation could occur in a fixed-price type contract.

77. On information and belief, at the time of the A-12 FSED Contract award, the government knew from other classified, special access, compartmented programs, that the significant research and development which would be necessary to reduce risks involved in the incorporation of key technologies into the A-12 aircraft to a level at which realistic pricing or an equitable and sensible risk allocation could occur in a fixed-price type contract had not been accomplished.

78. On information and belief, at the time of the A-12 FSED Contract award, the government possessed information from other programs that was not available to the Contractors, and that indicated the Contractors' planned development approach to several key technologies would not achieve the requirements of the specifications.

79. On information and belief, at the time of the A-12 FSED Contract award, the government knew that the contractual schedules contemplated for development of those technologies in the A-12 program would be inadequate, and that a significant extension of the Contract delivery schedule would be necessary to complete the necessary research and development effort.

80. On information and belief, the Navy officials responsible for the A-12 program, including the procuring contracting officer, knew at the time of

the A-12 FSED Contract award that the Department of Defense, through its senior officials, opposed the use of a fixed-price type contract for A-12 FSED because, inter alia, technical, schedule and price risks had not been reduced sufficiently to permit lawful use of a fixed-price type contract.

81. On January 13, 1988, after award of the Contract, the Navy advised the Contractors of the Navy's assessment of projected A-12 performance in several key categories. The Navy's projected performance of the aircraft did not meet A-12 FSED Contract specification requirements in all cases, but nonetheless the projected performance of the A-12 was accepted by the Navy as a basis for award of the Contract. At the time the Contract was terminated, the Contractors' performance status, based on the then current A-12 weight projection, was equal to or better than the Navy's assessment at the time of award, or the A-12 specification requirements, in each of the evaluated categories. (*See* paragraph 176.)

82. [This paragraph set forth in classified annex]

83. The Contract purported to require the Contractors to design, develop, manufacture and deliver eight FSED aircraft and associated mock-ups, models and test articles in accordance with the Detail Specification for the ATA, SD-574-1. Detail Specification SD-574-1 was based on and closely followed Type Specification TS-185.

84. At the time of Contract award, the Contract also required the Contractors to complete

an Initial Design Review not later than six months after Contract award, for which the Contractors were to be paid $244,150,654, a Preliminary Design Review not later than twelve months after Contract award, for which the Contractors were to be paid $236,957,522, and a Critical Design Review eighteen months after Contract award, for which the Contractors were to be paid $504,160,441.

85. The Contract also contained options for the delivery of production aircraft in Lots I through IV. Lot I consisted of six aircraft; Lot II, eight aircraft; Lot III, twenty aircraft; and, Lot IV, thirty-six aircraft. The option quantities of aircraft for Lots I-III were priced at not-to-exceed values of $928,525,133, $1,039,792,714, and $1,644,737,657, respectively. Lot IV option quantities of aircraft were to be priced during performance of the A-12 FSED Contract, at not greater than the unit price for Lot III aircraft. The Contract also permitted the Navy to vary the option quantities with corresponding adjustments to the option prices.

86. In the original FSED Contract, delivery of the first ATA FSED aircraft was to take place in June 1990, with subsequent FSED aircraft deliveries occurring from July 1990 through January 1991. Option quantities, if validly exercised by the Navy, were to be delivered commencing in June 1991.

87. Clause H-7 of the Contract, entitled "Allotment of Funds Applicable to FSED Items," provided for incremental funding of the Contract. Clause H-7 acknowledged the unavailability for obligation, at the time of Contract award, of

sufficient funds to cover either the target value or the ceiling price of the basic FSED contract line items. Clause H-7 also provided that the Contract neither authorized nor required the Contractors to incur costs during performance of the Contract, plus a reasonable allowance for profit, in excess of the total amount obligated to the Contract at any given time.

The Contractors' Performance of the A-12 FSED Contract

88. During performance of the A-12 FSED Contract, the Contractors experienced significant difficulties caused by various acts and omissions of the Navy. These Navy-caused difficulties severely affected the schedule within which the Contractors could complete the required FSED and Lot I tasks, as well as the costs of performance.

Impossibility of Achieving Specified Aircraft Weight

89. The A-12 FSED Contract purported to require the Contractors to develop an aircraft meeting a specified empty weight, which was based on the Contractors' initial projections of the aircraft weight.

90. The Navy expected at the time of Contract award that the A-12 aircraft weight would exceed the specification weight requirement by at least 2631 pounds, and, on information and belief, knew that the specification weight requirement was unachievable.

91. The Navy expected to revise the specification weight and other requirements as necessitated by the development effort.

92. The Navy had a duty not to withhold unreasonably approval of revisions to weight and other specifications necessitated by the development effort. The Navy also had a duty to accept promptly such revisions so as not to impede the development effort.

93. Because of similarities in configuration, materials and technology, the government knew that the B-2 aircraft was the only comparable aircraft that could have been used as a basis for accurate A-12 weight prediction. The government, through its security constraints, made it impossible for the Contractors to obtain or use B-2 information for this purpose. As a result, the Contractors were forced to rely on incomplete information that nonetheless was the best available to the Contractors. The Contractors therefore substantially underestimated the weight of the A-12 at the time the best and final offer was submitted.

94. The government failed to disclose to the Contractors its knowledge of information, exclusively within its possession or control, relating to weight estimation techniques for a modern low observable, thick wing aircraft utilizing extensive composite material construction.

a. The government failed to disclose the bases for its statements, both before and after Contract award, that the A-12 aircraft weight would

be significantly higher than that predicted by the Contractors.

b. The government failed to disclose its knowledge of structural weight estimation techniques and manufacturing technologies associated with the unconventional, low observable, flying wing configuration of the A-12 aircraft.

c. The government failed to disclose its knowledge of structural weight estimation and manufacturing technologies associated with the extensive use of advanced composite materials on the A-12 aircraft.

95. The Navy required the Contractors to perform extensive and costly weight reduction efforts. Through the date of termination, the Contractors were required to expend extraordinary amounts of resources to contain and reduce weight in the aircraft, and they were unable ever to satisfy the original A-12 weight specification.

96. Moreover, the Navy directed the Contractors to reanalyze and redesign the aircraft to reflect increased Navy weight estimates.

97. The Contractors incurred substantial costs and delays in completing studies and changes in, aircraft design which successfully minimized the effect of additional weight on aircraft performance.

98. These reanalysis and redesign efforts caused substantial delay in the release of engineering structural drawings, and otherwise disrupted the Contractors' performance.

99. The multiple reanalysis and redesign efforts were unnecessary to satisfy the Contract requirements for the FSED phase.

100. The Navy unreasonably rejected more than half of the Contractors' weight reduction recommendations, thereby negating the Contractors' efforts to reduce the weight of the aircraft, and causing additional costs and delay to the Contractors' performance.

101. By the fall of 1989, the Contractors concluded that the empty weight of the aircraft would exceed the specification requirement by approximately 3800 pounds, and that no further significant weight savings were commercially practicable to achieve, without changes to other specification requirements.

102. Test data and analysis demonstrated the A-12 would satisfy the Navy's operational needs even with the predicted weight increase. On that basis, the Navy accepted the predicted weight increase of the aircraft.

103. In September 1989, the Navy expressly acknowledged the impossibility of achieving the A-12 weight specification, and stated that a "minimum weight" aircraft had been designed by the Contractors.

104. The Navy invited the Contractors to submit a formal proposal to revise the specifications to reflect the actual weight of the aircraft then predicted by the Contractors and acknowledged by the Navy.

105. Subsequently, the Navy unreasonably instructed the Contractors not to submit a formal proposal to modify the weight specifications.

Legal Impossibility of Achieving Low Observable Propulsion System

106. The specifications for the A-12 FSED Contract contained numerous interrelated requirements affecting the design of the A-12 propulsion system. Among the most important of these specifications were range, wind over deck, single engine rate of climb, weapons and fuel payload, and overall low observable radar and infrared signature.

107. Insufficient time and funding were provided by the Navy during the demonstration and validation phase of the A-12 Program to test adequately proposed designs of the propulsion system. Adequate testing before the FSED phase would have revealed to the Contractors that it was impossible or commercially impracticable to meet all specification requirements concurrently. Two of the areas that severely affected the time and cost of the Contractors' performance were the engine inlet and the exhaust nozzle.

Engine Inlet

108. The Navy's specification requirements, as they applied to the A-12 engine inlet, were collectively impossible or commercially impracticable to achieve.

109. The Contractors' FSED design was based on limited, half-scale test data resulting from

the Navy's compressed schedule and reduced funding for the demonstration/validation phase of the program. Further, the Contractors did not have access to data from other advanced programs, such as the B-2, which, on information and belief, could have permitted the Contractors to avoid the significant costs, as well as delay and disruption, associated with their efforts to comply with the Navy's specification requirements regarding the engine inlet.

110. From September 1988 until April 1990, the Contractors engaged in extensive and costly analysis, redesign and testing of the A-12 engine inlet, seeking to satisfy the impossible or impracticable specification requirements, and, ultimately, to advance the state-of-the-art.

111. Despite extensive engineering and testing efforts, the Contractors concluded that it is legally impossible or commercially impracticable to design an inlet that completely satisfied all of the Navy's specification requirements.

Exhaust Nozzle

112. The Navy's specification requirements, as they applied to the engine exhaust nozzle, were collectively impossible or commercially impracticable to achieve.

113. At the time the Contractors were testing a potential nozzle configuration during the demonstration and validation phase of the A-12 Program, the Contractors made repeated requests to the Navy for information relating to low observable

nozzle design that was, on information and belief, available to the Navy from other classified low observable weapons system programs. The information sought encompassed anticipated engine exhaust temperature profiles, thermal barrier materials, and implementations of low observability features. The Navy failed to respond to these requests.

114. The Contractors' use of a multilouver ejector nozzle design on the A-12 was dictated by the Navy's specification requirements, especially those relating to tail-on infrared signature. The multilouver configuration proposed by the Contractors assumed moderate exhaust temperatures, and used materials appropriate to those predicted temperatures.

115. The government gave the Contractors no indication that the Contractors were incorrect in assuming that moderate exhaust temperatures would be encountered.

116. Because of the Navy's highly compressed demonstration and validation schedule, neither full scale radar cross section nor comprehensive aerodynamic/propulsion testing of the exhaust system configuration had been conducted at the time the A-12 FSED Contract was awarded. The Navy's demonstration and validation phase funding and schedule limitations precluded full-scale radar cross section nozzle testing of the multilouver ejector nozzle until after award of the FSED Contract.

117. Full-scale radar cross section nozzle tests conducted in September 1988 revealed the

impossibility of attaining the specification requirements within the state-of-the-art.

118. Extensive testing then continued using full scale models to identify potential configuration changes. Many hours of aerodynamic and thermodynamic testing were required in excess of that reasonably projected at the time of award to identify an acceptable exhaust system configuration. As a result, the Contractors incurred substantial design and development costs relating to the exhaust nozzle to advance the state-of-the-art.

119. The final nozzle configuration represents an advance in the state-of-the-art.

120. The Contractors also were required to develop technology for certain thermal barrier materials. On information and belief, the government knew or was aware of thermal barrier technology developed and in existence on other programs, but failed to provide such information to the Contractors.

121. The failure of the government to disclose vital information regarding exhaust temperatures and thermal barrier development problems and solutions adversely affected the Contractors, requiring them to expend substantial resources to advance the state-of-the-art and to reinvent technologies to which, on information and belief, the government already had access.

Deficient Radar Supplier

122. The Navy's specification for the A-12 radar heavily favored a particular supplier that was

then developing a radar on another Navy aircraft program. The Navy insisted on that specification despite the Contractors' objection to its restrictive nature.

123. The Contractors selected that supplier as their A-12 radar subsystem subcontractor, without knowledge of that company's deficient performance on the other radar subcontract.

124. The Navy failed to disclose knowledge within its possession that the radar subsystem supplier's performance on the related ongoing radar subcontract was unsatisfactory and substantially behind schedule. That information was not available to the Contractors.

125. The radar subcontractor failed to make adequate progress toward timely completion of the A-12 radar subcontract.

126. The Contractors therefore terminated the radar subcontract on April 14, 1989, and were forced to reprocure the A-12 radar system from another supplier.

127. The Navy's failure to warn the Contractors of the radar supplier's previous deficient performance disrupted the Contractors' efforts under the A-12 FSED Contract, and increased their costs of performance.

Legal Impossibility of Achieving the Avionics Specifications

128. The Navy's specification requirements, as they relate to avionics subsystem antennas, were collectively impossible to achieve.

129. The government failed to disclose to the Contractors its knowledge of information relating to avionics antenna designs incorporating low observability features. On information and belief, this information was available to the Navy from, for example, the B-2 program, but was not available to the Contractors from any source.

130. The Navy modified its avionics specifications after Contract award to permit specification relaxation, on a case-by-case basis, in recognition of the impossibility of the performance of the original specification requirements.

131. By late July 1988, the Navy expressly acknowledged the impossibility of meeting the Contract specifications applicable to avionics subsystem antennas.

132. Nevertheless, the Navy unreasonably failed at any time to accept the case-by-case specification relaxation to avionics subsystem requirements when requested by the Contractors.

133. The Navy unreasonably required the Contractors to conduct extensive research and development to advance the state-of-the-art in low observable antenna design.

Navy Interference with Performance and Constructive Changes

134. During performance of the A-12 FSED Contract, the Navy failed to cooperate with the Contractors and actively interfered with and hindered the Contractors' performance. For example:

a. The Navy unreasonably and repeatedly delayed the approval of, arbitrarily disapproved, or withdrew prior approval of design decisions and requirements that were important to the accomplishment of FSED delivery schedules. Timely approval would have permitted the Contractors to reduce cost, reduce weight and improve aircraft performance.

b. The Navy unreasonably withheld or delayed approval of documents and data items submitted by the Contractors.

c. The Navy unreasonably failed to provide timely Material Review Board action for FSED aircraft components. The Navy also unreasonably failed to provide or delayed Material Review Board approval for components that were acceptable for FSED aircraft.

d. The Navy unreasonably impeded progress by denying the Contractors the flexibility to make prudent and reasonable configuration decisions on early FSED aircraft consistent with test requirements and objectives for these aircraft.

e. The Navy required repetitive analyses of projected aircraft loads, and required

unnecessary structural redesign to accommodate the Navy's weight projections that exceeded the Contractors' projected weight of the aircraft.

f. The Navy failed to resolve technical issues created by the Contract specifications in a timely manner.

g. The Navy failed to supply crucial information necessary to complete the design in a timely manner.

h. The Navy failed to provide access to other Department of Defense classified programs to the Contractors, such as the B-2, in a timely manner.

i. The Navy unreasonably imposed excessive formal redesign requirements.

j. The Navy imposed unreasonably stringent security requirements.

k. The Navy unreasonably directed that tasks not necessary for first flight of the aircraft nevertheless be completed before first flight.

l. The Navy failed to acknowledge or approve the Contractors' reasonable planned methods for accelerating performance to mitigate the effects of Navy-caused delay and disruption.

135. Navy acquisition policies in effect during the A-12 program directed that changes during development programs be kept to a minimum.

136. During performance of the A-12 FSED Contract, the Navy made formal and constructive changes to the specifications and to the Contractors'

reasonable planned methods of performance without granting equitable adjustments to the price or schedule of the A-12 FSED Contract. For example:

a. The Navy changed the Contract specifications by requiring the Contractors to provide support for the Aircrew Systems Advisory Panel beyond the level stated in the Contract.

b. The Navy constructively changed the Contract specifications to require materials and methods desired by the Navy but not required by the Contract.

c. The Navy unreasonably imposed additional non-destructive inspection and testing requirements that significantly increased the effort required to test the aircraft parts.

d. The Navy changed the Contract specifications by imposing auxiliary power unit exhaust gas temperature limitations.

Delay and Disruption

137. The Navy's conduct described in paragraphs 88 through 136 substantially delayed and disrupted the Contractors' performance of the A-12 FSED Contract.

138. For example, Navy-directed redesign efforts caused delays in the release of engineering drawings, delays and changes in tool design and tool fabrication, and delays and changes to, and scrapping of, aircraft components.

139. The Contractors' efforts to accommodate the Navy's conduct described in paragraphs 88

through 136 also resulted in reduced efficiency, performance of work out-of-sequence, and significant interruptions of planned work flows. For example, the Contractors hired and trained manufacturing employees to be available in accordance with the original FSED Contract schedule. When the government-caused delays became apparent, those employees had to be reassigned or laid off.

140. The Navy also forced the Contractors to perform without recognizing the cost and schedule impact of the Navy's actions. The Navy's failure to recognize necessary schedule adjustments required acceleration of the Contractors' efforts, further disrupting and increasing the cost of those efforts.

The Navy's Purported Option Exercise

141. By letter dated April 18, 1990, the Contractors informed the Navy that the Contract Lot I production option no longer described the A-12 aircraft then sought by the Navy, nor did the option set forth a price or delivery schedule consistent with the parties' intentions. The Contractors informed the Navy that the issues addressed in the A-12 Design Reviews, including weight and aircraft performance, precluded exercise of the Lot I option as that option was stated in the Contract.

142. By Modification P00045, dated May 31, 1990, the Navy purported to exercise unilaterally its option to purchase six Lot I initial production aircraft at the not-to-exceed price. The Navy failed to address any of the issues raised by the Contractors in their April 18, 1990 letter prior to the attempted option exercise.

143. By letter dated August 3, 1990, the Contractors objected to the Navy's purported exercise of the Lot I option, and proceeded with Lot I-related performance under protest. The letter stated that the technical impossibilities and commercial impracticabilities encountered by the Contractors were not recognized in the Navy's purported option exercise.

Waiver of A-12 FSED Contract Delivery Schedule

144. On information and belief, by no later than August 1989, the Navy had concluded that the schedules set forth in the A-12 FSED Contract for deliveries of FSED and production Lot I aircraft were not achievable.

145. After that time, the Navy indicated to the Contractors that time was not of the essence, and that it had elected to continue the program despite the recognition of unrecoverable delays in the FSED and Lot I delivery schedules.

146. By Modification P00046, dated August 17, 1990, the Navy purported unilaterally to re-establish a contractual delivery schedule for FSED aircraft. Under the Navy's unilateral schedule, FSED aircraft deliveries were to commence in December 1991. The Navy's unilateral schedule did not purport to alter the delivery schedule for the Lot I option.

147. By letter dated August 20, 1990, the Contractors objected to the Navy's proposed schedule as being unreasonable, and stated their intent to

continue performance on a reasonable schedule pending negotiation of a valid contractual delivery schedule while reserving all rights and remedies available to the Contractors.

148. By no later than September 21, 1990, the Navy concluded that the FSED delivery schedule set forth in Modification P00046 was not achievable by the Contractors and was not of essence to the Navy. The Navy indicated to the Contractors that the Navy had elected to continue the program notwithstanding the Navy's projected delays beyond the Modification P00046 FSED delivery schedule.

Reduction of Progress Payments

149. On September 27, 1990, in accordance with the terms of the Contract, the Contractors submitted Request for FSED Progress Payment No. 32. The Contractors requested the payment of $258,649,262 based on the costs incurred by the Contractors, the applicable progress payment rate, and payments already received.

150. The government wrongfully applied a "loss ratio" of 90.4% to the Contractors' FSED Progress Payment Request No. 32. The government deducted $199,559,499 from the Contractors' request and made a progress payment of only $64,089,763.

151. The government's use of a loss ratio wrongfully assumed the Contractors were at that time obligated to complete performance under the Contract, assumed the Contract would be completed at a loss to the Contractors, and reduced the progress

payments, allegedly in proportion to the estimated loss at completion.

152. On October 12, 1990, the Contractors submitted Request for FSED Progress Payment No. 33. The Contractors requested the payment of $245,178,636.

153. The government wrongfully applied a loss ratio of 90.4% to FSED Progress Payment Request No. 33. The government deducted $199,107,368 from the Contractors' request and made a progress payment of only $46,071,268.

154. On November 7, 1990, the Contractors submitted Request for FSED Progress Payment No. 34. The Contractors requested the payment of $275,094,203.

155. The government wrongfully applied a loss ratio of 87.7% to FSED Progress Payment Request No. 34. The government deducted $264,196,077 from the Contractors' request and made a progress payment of only $10,898,126.

Insufficient Obligation of Funds to the A-12 FSED Contract

156. By approximately mid-July 1990, the Contractors' incurred costs, commitments to incur future costs, and termination liability for the FSED portion of Contract exceeded the funds obligated to the FSED portion of the Contract.

157. By letter dated September 5, 1990, the Contractors advised the Navy that the Navy had not obligated to the Contract sufficient funds to cover the

Contractors' costs, including termination liability. The Contractors requested that the Navy obligate additional funds to the Contract while reserving all rights and remedies available to the Contractors.

158. By letter dated October 3, 1990, the Navy responded to the Contractors' request, contending that "all Government obligations under the Allotment of Funds clause have been met and the Contractor team has a duty to satisfy its obligations."

The Contractors' Request for A-12 FSED Contract Restructure

159. On November 12, 1990, the Contractors submitted to the Navy a Memorandum in Support of Request for Contract Restructure. The Contractors requested reformation of the A-12 FSED Contract including restructuring of the price, terms and conditions, specifications, and schedule.

160. Thereafter, the Navy and the Contractors engaged in negotiations over a restructured contract that resulted in an agreement by the Navy to recommend contract restructure to the Department of Defense.

The Navy's Termination of the A-12 FSED Contract

161. On December 14, 1990, the Secretary of Defense issued an internal memorandum directing the Secretary of the Navy to show cause why the A-12 FSED Contract should not be terminated. The Secretary's memorandum expressed concern that the cost growth of the program was "intolerable."

162. By letter dated December 17, 1990, the Navy issued to the Contractors a "Cure Notice" contending that the Contractors had failed to fabricate parts sufficient to permit final assembly in time to meet FSED delivery schedules, and that the Contractors would not deliver the Lot I option quantity of aircraft in accordance with the Contract delivery schedule. The Cure Notice also alleged that the Contractors' failure to meet specification requirements "such as weight" jeopardized the "carrier suitability" of the A-12 design. The Cure Notice required that the deficiencies be "cured" by January 2, 1991.

163. On December 31, 1990, the Contractors submitted certified claims for equitable adjustments to the price and schedule of the Contract by reason of contract formation and performance issues and the Navy's use of an improper contract type. The Contractors' claims asserted entitlement to equitable adjustments as the result of the Navy actions set forth in the preceding paragraphs.

164. By letter dated January 2, 1991, the Contractors responded to the Cure Notice, stating that they were not in default. The Contractors noted that the Contract delivery schedules were unenforceable, and asserted entitlement to extensions of the Contract delivery schedules on the grounds set forth in the Contractors' Memorandum In Support of Request for Contract Restructure, submitted on November 12, 1990. The Contractors noted that the Navy found the A-12 design to be technically acceptable during the Critical Design

Review conducted under the Contract, and that the weight specification in particular was by then recognized by all parties to be impossible to achieve and was not of the essence. Finally, the Contractors detailed the significant progress being made by the Contractors to assure satisfactory completion of the Contract.

165. On information and belief, prior to termination, the Navy had accepted the Contractors' A-12 design, including its projected weight increase above the specification value, its projected performance in the areas addressed by the Contract specification with projected aircraft delivery dates later than those set forth in the Contract and the Contract modifications.

166. Prior to Contract termination, the Navy acknowledged the technical suitability of the A-12 aircraft design as it had been demonstrated through formal design reviews under the Contract. By the end of November 1990, all issues were resolved to the Navy's satisfaction.

167. On information and belief, prior to termination, the Navy acknowledged the acceptability of the FSED delivery schedule to which the Contractors were performing.

168. On information and belief, prior to termination the Navy failed adequately to consider whether the Contractors had experienced excusable causes of delay and were not in default.

169. On information and belief, prior to termination the Navy failed to account for the

Contractors' ability to accelerate aircraft assembly schedules by increasing work shifts and work days.

170. On information and belief, prior to termination the Navy recommended to the Secretary of Defense that the A-12 FSED Contract not be terminated. To the contrary, on information and belief, the Navy recommended that the Contract be reformed as requested by the Contractors.

171. On information and belief, on or about January 5, 1991, the Secretary of Defense ordered the A-12 FSED Contract be terminated, notwithstanding the Navy's recommendation not to terminate the Contract.

172. On information and belief, the decision to terminate the Contract was based on reasons other than the Contractors' performance of Contract requirements.

173. On information and belief, the termination for default did not reflect the independent determination of the contracting officer or the Navy that such action was appropriate.

174. By letter and Contract Modification, each dated January 7, 1991, the Navy purported to terminate the Contract for the alleged default of the Contractors. The termination was stated to be based on the Contractors' alleged inability to complete the design, development, fabrication, assembly, and testing of the A-12 aircraft within the Contract schedule. The termination also was stated to be based on the Contractors' alleged inability to meet the specification requirements for aircraft weight.

175. At the time the Contract was terminated, the Contractors were prosecuting the work towards timely completion of the A-12 FSED Contract and so as not to endanger performance of the Contract.

176. At the time the Contract was terminated, projected A-12 performance in several of the categories originally evaluated by the Navy at the time of award equaled or exceeded the contract specifications. At the time the Contract was terminated, projected A-12 performance in the remaining categories, based on the then current A-12 weight projection, equaled or exceeded the Navy's original projections of A-12 performance that formed the basis for the award of the Contract. (See paragraph 81.)

COUNT I

Award in Violation of Law Contract Void or Voidable

177. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

178. The Navy's use of a fixed-price type development contract for A-12 FSED was contrary to the requirements of Department of Defense Directive 5000.1, and related acquisition regulations. Use of a fixed-price contract type was, therefore, improper and unlawful.

179. In accordance with Section 8118 of the Department of Defense Appropriations Act, Pub. L. No. 100-202, 101 Stat. 1329, 1329-84 (1987) ("Section 8118"), and related provisions in FY 1989 (Section

8085 of the Department of Defense Appropriations Act, 1989, Pub. L. No. 100-463, 102 Stat. 2270, 2270-32 (1988) ("Section 8085")), FY 1990 (Section 9048 of the Department of Defense Appropriations Act, 1990, Pub. L. No. 101-165, 103 Stat. 1112, 1139 (1989) ("Section 9048")), and FY 1991 (Section 8037 of the Department of Defense Appropriations Act, 1991, Pub. L. No. 101-511, 104 Stat. 1856, 1882-83 (1990) ("Section 8037")), none of the funds appropriated by Congress to the Department of Defense in FY 1988 through FY 1991 could be obligated or expended for fixed-price type contracts in excess of $10 million for the development of a major system, unless the Under Secretary of Defense for Acquisition determined that program risk had been reduced to the extent that realistic pricing could occur, and that the contract type presented an equitable and sensible allocation of program risk between the contracting parties.

180. On information and belief, the government obligated and expended funds subject to Section 8118, Section 8085, Section 9048, and Section 8037 on the A-12 FSED Contract.

181. On information and belief, the Under Secretary of Defense for Acquisition failed to make the determination required by Section 8118 prior to award of the A-12 FSED Contract. On information and belief, the Under Secretary of Defense for Acquisition also failed to make the determinations required by Sections 8085, 9048 and 8037 at any time after the award of the A-12 FSED Contract.

182. Any purported Section 8118, 8085, 9048 or 8037 determination rendered by the Department

of Defense on the A-12 Program is of no force and effect, in view of the level of program risk that was known to the government at the time such a determination was made.

183. In the absence of a proper determination under Section 8118, FY 1988 funds were not available for award of the fixed-price A-12 FSED Contract, and the award therefore violated the Antideficiency Act, 31 U.S.C. § 1341, and 41 U.S.C. § 11, by creating a contract and obligation in the absence of and in excess of available appropriations.

184. In the absence of proper determinations under Sections 8085, 9048 and 8037, FY 1989, 1990, and 1991 funds, respectively, were not available for obligation to the A-12 FSED Contract, and the Navy's insistence on the Contractors' continued performance under the Contract created additional obligations in the absence of and in excess of available appropriations, in violation of the Antideficiency Act, 31 U.S.C. § 1341, and 41 U.S.C. § 11.

185. The Navy's failure to obtain proper determinations under Sections 8118, 8085, 9048 and 8037, its use of a fixed-price type of contract in the absence of such proper determinations, and its failure to adhere to DOD Directive 5000.1 and related regulations, rendered the A-12 FSED Contract and its production options void ab initio, or, in the alternative, voidable, or subject to reformation.

186. The Navy benefited from the Contractors' A-12 Program-related efforts, and their

substantial progress toward development of the A-12 aircraft. On information and belief, the Navy intends to use technical information developed under the A-12 FSED Contract in future Navy aircraft development and modification programs.

187. The government's acceptance of these benefits created a contract implied-in-fact under which the Contractors must be compensated.

188. The Navy failed adequately to compensate the Contractors under this Contract in accordance with their efforts.

COUNT II
[Title set forth in classified annex]

189. Plaintiffs reallege paragraphs 1-176 and 178-188 as if set forth in their entirety.

190. [This paragraph set forth in classified annex]

191. [This paragraph set forth in classified annex]

192. [This paragraph set forth in classified annex]

193. Accordingly, the A-12 FSED Contract was awarded in violation of law and was, therefore, void ab initio, or in the alternative, voidable.

194. [This paragraph set forth in classified annex]

195. Accordingly, the A-12 FSED Contract was void or voidable, or subject to reformation, after the expiration of fiscal year 1988.

196. The Navy benefited from the Contractors' A-12 Program-related efforts, and their substantial progress toward development of the A-12 aircraft. On information and belief, the Navy intends to use technical information developed under the A-12 FSED Contract in future Navy aircraft development and modification programs.

197. The government's acceptance of these benefits created a contract implied-in-fact under which the Contractors must be compensated.

198. The Navy failed adequately to compensate the Contractors under this contract in accordance with their effort.

COUNT III

Incremental Funding
Contract Void or Voidable

199. Plaintiffs reallege paragraphs 1-176 and 178-188 as if set forth in their entirety.

200. The A-12 FSED Contract provided that funds were to be obligated to the Contract on an "installment" basis, pursuant to a funding schedule set forth in Clause H-7 of the Contract.

201. The government is prohibited from awarding a fixed-price contract when less than the total contract price is obligated to the contract at the date of award, because such an award attempts to create a contract and obligation in excess of available appropriations. 31 U.S.C. §§ 1341-1342; 41 U.S.C. § 11 (1988). The government is thus prohibited from

awarding a fixed-price contract with funding to be obligated on an installment basis.

202. The A-12 FSED Contract was awarded without funding adequate to cover the FSED tasks priced in the Contract, in violation of the statutes cited in paragraph 196.

203. Accordingly, the A-12 FSED Contract was awarded in violation of law and was, therefore, void ab initio, or, in the alternative, voidable, or subject to reformation.

204. The Navy benefited from the Contractors' A-12 Program-related efforts, and their substantial progress toward development of the A-12 aircraft.

205. The government's acceptance of these benefits created a contract implied-in-fact under which the Contractors must be compensated.

206. The Navy failed adequately to compensate the Contractors under this contract in accordance with their efforts.

COUNT IV

Contractors Not In Default
Incremental Funding
Best Efforts Performance Obligation

207. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

208. Funding of the Contract by the Navy up to the Contract price was a condition to any obligation on the part of the Contractors to complete the work under the A-12 FSED Contract.

209. The Navy failed to fund the Contract up to the Contract price.

210. Prior to obligation of the total Contract price by the Navy, the Contractors' obligation was to use their best efforts in expending obligated funds toward the objectives of the Contract, just as if the Contract were cost-type in nature.

211. The Contractors expended Contract funds using their best efforts and diligently pursued the objectives of the Contract.

212. The Navy was not entitled to assess the Contractors' progress or prosecution of the work as if the A-12 FSED Contract had been funded up to the Contract price, and as if the Contractors had an unconditional obligation to complete the Contract.

213. Therefore, the Contractors were not in default of their A-12 FSED and Lot I Contract obligations at the time the Contract was terminated.

214. The Navy wrongfully assessed the Contractors' progress and prosecution of the work as if the Contractors had an obligation to complete the A-12 FSED Contract despite the lack of funding.

215. The Navy wrongfully applied a loss ratio to Progress Payment Request Nos. 32 through 34 as if the Contractors had an obligation to complete the A-12 FSED Contract despite the lack of funding. The Navy's failure to make due and owing progress payments was a breach of the A-12 FSED Contract.

216. The Navy wrongfully terminated the A-12 FSED Contract for default, based on its improper assessment of the Contractors' progress and prosecution of the work.

COUNT V

Contractors Not in Default
Contractors' Right Not to Incur Costs in Excess of Obligated Funds

217. Plaintiffs reallege paragraphs 1-176 and 208-216 as if set forth in their entirety.

218. Pursuant to the incremental funding provisions of the Contract, "[n]othing herein shall authorize nor require the Contractor[s] to incur costs, plus a reasonable allowance for profit, in excess of the total amount obligated at any given time." Contract Clause H-7.

219. Contract funds are exhausted when the sum of the Contractors' incurred costs, plus its commitments to incur costs in the future, plus any other costs that would be expected to be incurred in the event of a contract termination for the convenience of the government, exceed the funds obligated to the Contract.

220. By mid-1990, the Contractors had exhausted the amount of funding obligated to the Contract.

221. The Navy failed, prior to or following the exhaustion of the obligated funds, to obligate additional funds adequate to finance the Contractors' performance.

222. By reason of the exhaustion of the incremental funding, the Contractors were entitled under the terms of the Contract to stop incurring costs by discontinuing performance until additional funds were obligated.

223. Without funding to support continued performance, the A-12 FSED Contract expired upon the Contractors' exhaustion of funding obligated to the Contract. 31 U.S.C. § 1341(a)(1)(B).

224. By its conduct, concluding with issuance of an alleged "Cure Notice" to the Contractors on December 17, 1990, the Navy sought to require the Contractors to continue performance in violation of the express terms of the Contract, even though no additional funds had been obligated to the Contract.

225. The Navy's requirement to "cure" or to continue performance at a time when obligated funding was exhausted violated 31 U.S.C. § 1342 (1988).

226. The Cure Notice issued on December 17, 1990, therefore, was defective.

227. At the time the Navy terminated the Contract, the Contractors were not in default of their A-12 FSED obligations by reason that, under the express terms of the Contract, the Contractors were not obliged to continue performance beyond the level of incremental funding then obligated to the Contract, and the Navy had no right to require performance in excess of the obligated funds.

228. The Navy wrongfully terminated the A-12 FSED Contract for default.

COUNT VI

Contractors Not in Default/Default Excusable Impossibility of Performance

229. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

230. During performance of the A-12 FSED Contract, the Navy's specification requirements, collectively, proved to be legally impossible to achieve.

231. The A-12 aircraft weight contained in the FSED Contract specifications proved to be legally impossible to achieve.

232. The A-12 aircraft propulsion and low observability requirements contained in the Contract specifications proved to be legally impossible to achieve.

233. The A-12 avionics and low observability requirements contained in the Contract specification, as they apply to certain aircraft antennas, proved to be legally impossible to achieve.

234. On information and belief, the government knew or had reason to know at the time of award of the A-12 FSED Contract that its specification requirements for the A-12 would prove to be legally impossible to achieve.

235. The legal impossibility of performing to the Navy's specifications was not due to the Contractors' lack of skill, judgment or know-how. Information from other classified government programs that would have enabled the Contractors

to recognize the impossibility of achieving the specifications was not disclosed to the Contractors.

236. Further, the Navy's compression and underfunding of the demonstration/validation phase of the A-12 program prevented the Contractors from discovering the impossibility of performance before award of the FSED Contract.

237. The Contractors did not assume the risk that the Navy's specification requirements would be legally impossible to achieve.

238. The Contractors' delays in performance and failure to achieve certain specification requirements were excusable, because they arose out of the Navy's imposition of specification requirements that were legally impossible to achieve.

239. The Contractors were not in default of their A-12 FSED and Lot I Contract obligations by reason of the Navy's imposition of A-12 specification requirements that were legally impossible to achieve.

240. The government wrongfully terminated the A-12 FSED Contract for default.

COUNT VII

Contractors Not in Default/Default Excusable Commercial Impracticability

241. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

242. During performance of the A-12 FSED Contract, the Navy's specification requirements, collectively, proved to be commercially impracticable to achieve.

243. Performance of FSED tasks required significantly more time to complete than the contracting parties contemplated at the time of award.

244. Performance of FSED tasks required significant amounts of unanticipated research and development not contemplated by the parties at the time of award.

245. Performance of FSED tasks required expenditure of costs greatly disproportionate to the FSED Contract price.

246. The A-12 aircraft weight contained in the FSED Contract specifications proved to be commercially impracticable to achieve.

247. The A-12 aircraft propulsion system and low observability requirements contained in the Contract specifications proved to be commercially impracticable to achieve.

248. The A-12 avionics and low observability requirements contained in the Contract specification, as they apply to certain aircraft antennas, proved to be commercially impracticable to achieve.

249. The composite manufacturing methods required to satisfy the A-12 Contract specification requirements, collectively, proved to be commercially impracticable to achieve.

250. On information and belief, the government knew or had reason to know at the time of award of the A-12 FSED Contract that its

specification requirements for the A-12 would prove to be commercially impracticable to achieve.

251. The commercial impracticability of performing to the Navy's specifications was not due to the Contractors' lack of skill, judgment or know-how. Information from other classified government programs that would have enabled the Contractors to recognize the commercial impracticability of achieving the specifications was not disclosed to the Contractors.

252. Further, the Navy's schedule compression and underfunding of the demonstration and validation phase of the A-12 program prevented the Contractors from discovering the commercial impracticability of performance before award of the FSED Contract.

253. The Contractors did not assume the risk that the Navy's specification requirements would be commercially impracticable to achieve.

254. The Contractors' delays in performance and failure to achieve certain specification requirements were excusable, because they arose out of the Navy's imposition of specification requirements that were commercially impracticable to achieve.

255. The Contractors were not in default of their A-12 FSED and Lot I Contract obligations by reason of the Navy's imposition of A-12 specification requirements that were commercially impracticable to achieve.

256. Accordingly, the government wrongfully terminated the A-12 FSED Contract for default.

COUNT VIII

Contractors Not in Default/Default Excusable Mutual Mistake of Fact

257. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

258. In the alternative, at the time of the award of the A-12 FSED Contract, the Contractors and the Navy believed that the specifications were achievable.

259. At the time of the award of the A-12 FSED Contract, the Contractors and the Navy believed that access to classified information relevant to aircraft configuration, composites, and, low observable technology, and vital to the Contractors' performance of the Contract, would be provided to the Contractors after contract award.

260. At the time of the award of the A-12 FSED Contract, the Contractors and the Navy believed that program risk had been reduced to a point where realistic pricing could be established for a fixed-price contract.

261. The parties were mistaken as to the factual premises for the foregoing beliefs.

262. The mistaken factual premises were fundamental assumptions of the A-12 FSED Contract.

263. The A-12 FSED Contract did not place the risk of the above mistakes on the Contractors

and the Contractors did not assume the risk of the mistakes.

264. Had the Navy been aware of the true facts at the time of the award of the A-12 FSED Contract, it would have agreed to a cost-reimbursement contract with achievable specifications.

265. The Navy has benefited from the Contractors' efforts and its substantial progress toward development of the A-12.

266. The parties' mutual mistakes of fact render the A-12 FSED Contract subject to reformation to a cost-reimbursement type contract.

267. Under the reformed Contract, the Contractors were making satisfactory progress at the time the Contract was terminated.

268. The government wrongfully terminated the A-12 FSED Contract for default.

COUNT IX

Contractors Not in Default/Default Excusable Failure to Disclose Superior Knowledge

269. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

270. The government failed to disclose its superior knowledge of information vital to the Contractors' performance of their A-12 FSED Contract obligations.

271. The government knew that vital information held by the government in classified,

compartmented weapon system development programs, was not available to the Contractors except as disclosed by the government. Moreover, the government's conduct misled the Contractors.

272. The Contractors were not in default of their A-12 FSED and Lot I Contract obligations by reason of the government's failure to disclose information vital to the Contractors' performance of their A-12 FSED Contract obligations.

273. The Contractors' delays in performance and their failure to achieve certain specification requirements were excusable, by reason of the government's failure to disclose its superior knowledge of information vital to the Contractors' performance of its A-12 FSED Contract obligations.

274. The government wrongfully terminated the A-12 FSED Contract for default.

COUNT X

Contractors Not in Default/Default Excusable Failure to Cooperate/Constructive Changes

275. Plaintiffs reallege paragraphs 1-176, 230-40, 242-56, and 270-74 as if set forth in their entirety.

276. The unreasonable conduct of the Navy in hindering and interfering with the Contractors' performance of the A-12 FSED Contract constitutes a breach of the Navy's duty to cooperate.

277. The Contractors were not in default of their A-12 FSED Contract obligations, by reason of the Navy's breach of its duty to cooperate and its

imposition of formal and constructive changes to the specifications and to the Contractors' planned methods of performance.

278. The Contractors' delays in performance were excusable, by reason of the Navy's breach of its duty to cooperate by, for example, establishing impossible or unreasonable specification requirements, and then insisting that the Contractors continue to attempt to achieve the requirements even after the impossibility of achieving them was recognized. The Navy also breached its duty to cooperate by imposing formal and constructive changes to the specifications and to the Contractors' planned methods of performance without equitably adjusting the Contract price and schedule, and by wrongfully withholding progress payments otherwise due and owing to the Contractors, based on the wrongful application of an adjustment for loss.

279. The Navy also breached its duty to cooperate by failing formally to modify specification values, such as those addressing A-12 weight, when such modifications would not affect the A-12's ability to accomplish the Navy's operational needs.

280. Under the schedule extensions to which the Contractors were entitled by reason of the excusable delays encountered in performance of the A-12 FSED Contract, the Contractors were making satisfactory progress at the time the Contract was terminated.

281. In light of the Navy's decisions: (1) to curtail funding, technical efforts, and performance

schedule for the demonstration and validation phase; (2) to limit funding obligated to the fixed-price type A-12 FSED Contract; and (3) not to disclose vital technical information generated by other government programs, the Navy had an affirmative duty to cooperate with the Contractors that included a duty timely to make any specification changes not inconsistent with the A-12's ability to perform the operational needs of the Navy, and to adjust the Contract performance schedule to account for such specification changes.

282. The government wrongfully terminated the A-12 FSED Contract for default.

COUNT XI

Contractors Not in Default/Default Excusable Breach of Implied Covenant of Good Faith and Fair Dealing

283. Plaintiffs reallege paragraphs 1-176, 230-40, 242-56, 270-74 and 276-82 as if set forth in their entirety.

284. The A-12 FSED Contract included an implied covenant of good faith and fair dealing, by which both parties agreed not to do anything that would deprive the other of the benefits of the Contract, including an implied promise by each party to refrain from doing anything that would render performance of the Contract impossible by any act of its own, and to do everything that the Contract presupposes it would do to complete the A-12 FSED Contract effort in a timely manner.

285. The Navy breached the implied covenant of good faith and fair dealing. For example:

a. The Navy unreasonably restricted the performance schedule and funding for the demonstration/validation phase of the A-12 Program, thus preventing the Contractors from performing vital risk reduction activities prior to award of the A-12 FSED Contract;

b. The Navy improperly selected a fixed-price type contract when it knew that risks had not been reduced to the extent required by law to permit proper use of that contract type;

c. The Navy imposed specification requirements that were impossible and/or commercially impracticable to achieve, and failed to incorporate in its specification its knowledge as to the achievability of those requirements or the suitability of particular estimation, design and fabrication methods.

d. The Navy warranted its specifications as being achievable, then failed to provide specification relief and equitable adjustments to the Contract price and schedule when it became apparent that the Navy's specifications were not achievable, and ultimately terminated the Contract on the basis of purported specification non-compliance;

e. The Navy failed to disclose its superior knowledge of information vital to the Contractors' performance and failed to grant access to other classified programs to Contractor personnel;

f. The Navy failed to cooperate, interfered with performance and imposed numerous constructive changes to the Contract amounting to a cardinal change;

g. The Navy wrongfully withheld progress payments otherwise due and owing to the Contractors, based on the wrongful application of an adjustment for loss;

h. The Navy wrongfully revived the weight specification as a pretext for terminating the Contract for default after repeatedly representing to the Contractors that compliance therewith was not of the essence, and after failing formally to modify the specification when such modification was necessary; and

i. The Navy wrongfully asserted the Contractors were not making progress or prosecuting the work in accordance with the Contract schedule, as a pretext for terminating the Contract for default, even though the Contractors were in fact making satisfactory progress and prosecuting the work in accordance with the Contract schedule.

286. As a result of the Navy's breach of the implied covenant of good faith and fair dealing, the government wrongfully terminated the A-12 FSED Contract for default.

COUNT XII

Contractors Not in Default
Lack of Enforceable Delivery Schedule (FSED)

287. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

288. By its conduct, the Navy waived the A-12 FSED Contract delivery schedule, and its right to terminate the A-12 FSED Contract for default based upon that schedule.

289. The Contractors relied on the Navy's election to continue the A-12 FSED Contract following the Navy's waiver of the Contract delivery schedule and proceeded with performance.

290. Under the reasonable schedule to which the Contractors were entitled, the Contractors were making satisfactory progress at the time the Contract was terminated.

291. The Navy failed to reestablish a reasonable and therefore enforceable delivery schedule. The schedule proposed by the Navy in Modification P00046 was not reasonable because, inter alia, it failed to take into account the design uncertainties remaining from the Critical Design Review, the Navy's ongoing failure to cooperate and imposition of constructive changes, and the Navy's restrictions on the Contractors' efforts to improve delivery schedules.

292. Even if Modification P00046 was an enforceable delivery schedule, the Navy waived the Modification P00046 delivery schedule and failed to

reestablish a reasonable and therefore enforceable delivery schedule.

293. The Contractors were not in default when the government terminated the Contract for alleged default.

294. The government wrongfully terminated the A-12 FSED Contract for default.

COUNT XIII

Contractors Not in Default
Lack of Enforceable Delivery Schedule (Lot I)

295. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

296. The Navy, by its conduct, waived the delivery schedule set forth for Lot I of the original A-12 FSED Contract.

297. The Navy failed to reestablish a reasonable and enforceable delivery schedule for Lot I aircraft.

298. The Contractors relied on the Navy's election to continue the A-12 FSED Contract following the Navy's waiver of the Contract delivery schedule and proceeded with performance.

299. Under the reasonable schedule extension to which the Contractors were entitled, the Contractors were making satisfactory progress at the time the Contract was terminated.

300. The Contractors were not in default when the Navy terminated the Contract for alleged default.

301. The government wrongfully terminated the Lot I portion of the A-12 FSED Contract for default.

COUNT XIV

Invalid Option Exercise

302. Plaintiffs reallege paragraphs 1-176 and 296-301 as if set forth in their entirety.

303. The Navy's attempt to exercise the option for Lot I aircraft in the A-12 FSED Contract was invalid. For example:

a. Completion of FSED aircraft deliveries prior to commencement of Lot I aircraft deliveries was an implied condition of the option. The government failed to satisfy this condition by attempting to exercise the Lot I Option with a schedule calling for deliveries of Lot I aircraft before completion of deliveries of FSED aircraft were due under the reasonable schedule to which the Contractors were then entitled.

b. The delivery schedule set forth in the option was known by the Navy to be impossible to achieve and was waived at the time of the attempted option exercise.

c. The Navy failed to exercise the option in strict accordance with its terms.

304. The Contractors were entitled to an equitable adjustment of the Contract option price and delivery schedule in recognition of the invalid option exercise. Alternatively, the Contractors performed their Lot I option efforts under an

implied-in-fact contract that was cost-reimbursement-plus-fixed-fee in nature.

305. Under the reasonable Lot I option performance schedule to which the Contractors were entitled, the Contractors were making satisfactory progress at the time the Contract was terminated.

306. The Contractors were not in default when the Navy terminated the Contract for alleged default.

307. The government wrongfully terminated the Lot I portion of the A-12 FSED Contract for default.

COUNT XV

Contractors Not in Default Contractors Prosecuting the Work

308. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

309. The Navy wrongfully asserted, in the termination notice issued January 7, 1991, that "the A-12 aircraft will not be delivered within the contract schedule."

310. At the time of the termination, the Contractors were prosecuting the work so as not to endanger performance of the A-12 FSED Contract and were making satisfactory progress towards completion of the design, development, fabrication, assembly and testing of the A-12 aircraft, in accordance with the Contract schedule, even as contained in Modification P00046.

311. Furthermore, the Navy constructively changed the delivery schedule contained in Modification P00046 to provide delivery schedule extensions.

312. At the time of termination, the Contractors were prosecuting the work so as not to endanger the performance of the A-12 FSED Contract and were making satisfactory progress towards completion of the design, development, fabrication, assembly and testing of the A-12 aircraft, in accordance with the Contract delivery schedule, as constructively changed by the Navy.

313. Accordingly, the Contractors were not in default.

314. The Navy wrongfully terminated the A-12 FSED Contract for default.

COUNT XVI

Contractors Not in Default
Waiver of Weight Specification

315. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

316. On information and belief, the Navy knew from the outset of the A-12 FSED Contract that the empty weight specification of the aircraft was not achievable.

317. The Navy had a contractual duty formally to modify the specification weight requirements.

318. By no later than September 1989, the Navy expressly informed the Contractors that strict

compliance with the weight specification stated in the Contract was not of the essence, because the operational needs of the Navy were satisfied with the aircraft at its then predicted weight. Accordingly, the Navy requested the Contractors to submit a proposal to change the specification to reflect the higher weight.

319. Because the aircraft weight satisfied the Navy's operational needs, the Navy intended to relax the weight specification in exchange for other consideration from the Contractors.

320. The Contractors relied to their detriment on the Navy's representations that strict adherence to the weight specification was not essential, and continued to perform the A-12 FSED Contract.

321. The Navy failed formally to modify the weight specification.

322. The Contractors were not aware that the government would later revive the A-12 weight specification as a pretext for terminating the Contract for default.

323. The Navy waived the Contractors' failure to satisfy the weight specification as a basis for terminating the A-12 FSED Contract for default.

324. The Navy wrongfully terminated the A-12 FSED Contract for default.

COUNT XVII

Contractors Not in Default
Violation of Termination Procedure

325. Plaintiffs reallege paragraphs 1-176, 288-94, 296-301, and 316-24 as if set forth in their entirety.

326. Federal Acquisition Regulation ("FAR") § 49.402-3(f) (48 C.F.R. § 49.402-3(f) (1990)) sets forth specific factors which a contracting officer must consider prior to reaching a decision to terminate for default.

327. On information and belief, the contracting officer failed adequately to consider the factors set forth in FAR § 49.402-3(f) before termination of the A-12 FSED Contract.

328. On information and belief, termination of the A-12 FSED Contract and Lot I option was directed by the Department of Defense.

329. On information and belief, the Department of Defense failed to review the circumstances of the Contractors' performance, but rather based its direction to terminate for default on grounds unrelated to the Contractors' performance of contractual requirements. Specifically, the Department of Defense failed to consider the Navy's determination that the forecast weight and anticipated delivery schedule for the A-12 as of the time of termination was acceptable and satisfied the Navy's operational needs.

330. On information and belief, the contracting officer did not make an independent decision pursuant to FAR § 49.402-3 prior to issuing the default termination notice.

331. The Department of Defense's order improperly removed from the contracting officer his decision-making authority, and deprived the Contractors of the contracting officer's independent decision on whether to terminate the Contract for alleged default.

332. The government wrongfully terminated the A-12 FSED Contract for default.

COUNT XVIII

Contractors Entitled to Equitable Adjustment

333. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

334. The Contractors are entitled to an equitable adjustment in the target price of the A-12 FSED Contract, and a corresponding adjustment to the Contract delivery schedule, as set forth in the Contractors' certified claims submitted on December 31, 1990, as updated thereafter.

335. The Navy wrongfully denied the Contractors' claims and refused to adjust the Contract price and schedule.

COUNT XIX

Estoppel to Rely on FSED Funding Cap

336. Plaintiffs reallege paragraphs 1-176 as if set forth in their entirety.

337. By approximately mid-July 1990, the Contractors' FSED incurred costs plus termination liability exceeded the funds obligated to the FSED portion of the Contract.

338. By no later than September 5, 1990, the contracting officer knew that the Contractors' incurred costs plus termination liability exceeded the funds obligated to the FSED portion of the Contract.

339. In June 1990 and repeatedly thereafter, the Contractors placed the Navy on notice that various acts and omissions of the Navy had resulted in constructive changes to the Contract, and had otherwise significantly increased the Contractors' costs of performance. These Navy acts and omissions also resulted in the Contractors' incurred costs plus termination liability exceeding the funds obligated to the FSED portion of the Contract.

340. Notwithstanding his knowledge that the Contractors had exhausted the funds obligated to the FSED portion of the Contract, the contracting officer directed and induced continued performance by the Contractors. For example:

a. By letter dated October 3, 1990, the contracting officer asserted that the Contractors had a duty to continue performance, in advance of the obligation of additional funds to the Contract.

b. The contracting officer issued formal letters of direction on October 3, 1990 and November 20, 1990 requiring the performance of additional effort in advance of the obligation of additional funds to the Contract.

c. The contracting officer issued a Cure Notice on December 17, 1990 requiring correction of purported deficiencies in the Contractors' performance in advance of the obligation of additional funds to the Contract.

341. On information and belief, the Navy intended these letters to be acted upon, and intended to induce the Contractors to continue performance on the Contract.

342. On information and belief, at the time the Contract was terminated, additional funds had been appropriated by Congress and were available to the Navy to be obligated to the A-12 FSED Contract.

343. The Contractors reasonably believed, based on the Navy's conduct, that the Navy would obligate funds to the A-12 FSED Contract sufficient to cover costs incurred in performing work required by the Navy after the funds obligated to the Contract had been expended.

344. Under the Contract, the Navy was scheduled to obligate additional funds to the FSED portion of the Contract on or before January 7, 1991. The Contractors' knowledge of the availability of these additional funds confirmed their belief that the Navy had available and intended to obligate sufficient funds to cover the additional performance directed by the Navy.

345. The Contractors relied on the conduct of the Navy inducing their continued performance on the A-12 FSED Contract, and expended substantial funds toward completion of the Contract tasks.

346. By its actions, the Navy is estopped from relying on the limitation of obligated funds on the Contract.

COUNT XX

Violation of Deferment Agreement By Demands For Repayment Of Unliquidated Progress Payments

347. Plaintiffs reallege paragraphs 1-346 as if set forth in their entirety.

348. On January 7, 1991, the Navy's contracting officer issued a final decision purporting to terminate the A-12 FSED Contract for default. Based on that final decision, on February 5, 1991 the Navy issued a demand in the form of a government claim for the return of unliquidated progress payments made to the Contractors during performance of the A-12 FSED Contract in the amount of $1.35 billion.

349. By issuing its demand for return of progress payments the contracting officer was required to follow a set of established procedures outlined by federal procurement regulations for agency determination and collection of a contract debt. In FAR Subpart 32.6, the contracting officer is required to determine whether a debt is due, negotiate the debt, and issue a demand for payment. See FAR §§ 32.606, 32.608, 32.610. In determining the amount of any contract debt, the contracting officer is required to consider both the government's claim, and any contract claims by the contractor against the government. FAR § 32.606(b).

350. After the contracting officer issues a demand for payment, FAR § 32.613 authorizes a contractor to request a deferment of collection of the debt. The FAR requires that the contracting officer "consider whether deferment of the debt collection is advisable to avoid possible overcollection. The responsible official may authorize a deferment pending the resolution of appeal." FAR § 32.613(d).

351. The FAR also provides that deferments pending disposition of a contractor's suit may be granted to financially weak contractors, with a reasonable balance of the need for government security against loss and undue hardship on the contractor. FAR § 32.613(e).

352. On February 5, 1991, the Contractors formally requested pursuant to FAR § 32.613 deferment of collection of the claimed amount. Acting on that request and on that same day, the Navy and the Contractors entered into an agreement (the "Deferment Agreement"), which defers collection and payment of the Navy's unliquidated progress payment claim pending the outcome of the Contractors' suit challenging the propriety of the termination of the A-12 FSED Contract for default. A true and correct copy of the Deferment Agreement is attached hereto as Exhibit B.

353. The Deferment Agreement is in full force and effect, and by its terms prevents the government from attempting to collect on its claim for unliquidated progress payments pending resolution of the disputed claim. The Deferment Agreement provides (at ¶ 2):

> The Government will take no action, except as otherwise hereinafter provided, to enforce collection of the amount demanded pending (a) a decision by the Armed Services Board of Contract Appeals or the Claims Court on the Contractors' appeal, or (b) a negotiated settlement by and between the Government and the Contractors without such decision. . . .

354. In their Complaint, the Contractors contested the government's claim for return of unliquidated progress payments, and made that claim the subject of the litigation. See First Uncl. Am. Compl. ¶¶ 8, 15, F.

355. At the time of the termination of the A-12 FSED Contract, the Contractors had, and continue to have, in their possession property, including parts, equipment, supplies and tools, that was acquired or produced by the Contractors for the purpose of performing the A-12 FSED Contract and that was allocable or properly chargeable to that contract (hereinafter "A-12 Progress Payment Property").

356. Shortly after termination of the Contract, the Contractors informed the Navy that they would mitigate their termination costs by disposing of A-12 Progress Payment Property on a reasonable basis, while making credit adjustments to the appropriate A-12 Contract accounts, pending resolution of this litigation. Thereafter, the Contractors made such dispositions of A-12 Progress

Payment Property while making appropriate adjustments to A-12 Contract accounts resulting from those dispositions.

357. On May 19, 1992, the Navy contracting officer directed the Contractors to comply with certain procedures for the disposition of A-12 Progress Payment Property, and demanded, relying upon subparagraph (d)(5) of the Progress Payments Clause of the A-12 FSED Contract, FAR § 52.232-16(d)(5), current repayment of unliquidated progress payments for past and future dispositions.

358. The Contractors attempted to reach a compromise on the disposition and repayment issues, but the Navy contracting officer adhered to his demands in a July 28, 1992 letter, in which he advised the Contractors that the Navy's position was not subject to compromise and that the Contractors must either comply with the Navy's payment demands or cease dispositioning A-12 Progress Payment Property.

359. On August 21, 1992, the contracting officer repeated the Navy's demand that the Contractors either repay unliquidated progress payments or cease dispositioning A-12 Progress Payment Property. Again, he advised the Contractors that the Navy's demands were not subject to compromise.

360. The contracting officer's letters of July 28, 1992 and August 21, 1992 constitute a final decision on the government's claim that the Contractors must currently repay unliquidated

progress payments upon each disposition of A-12 Progress Payment Property.

361. On August 26, 1992, in response to the Navy's direction and under protest, General Dynamics and MDC forwarded checks to the Navy in the amounts of $4,368,260.58 and $54,414.00, respectively, representing the amounts of unliquidated progress payments claimed by the Navy to be due with respect to certain dispositions of A-12 Progress Payment Property. On August 26, 1992, the Contractors submitted a written, certified claim for $4,422,674.58, the total of those payments, to the contracting officer.

362. On October 23, 1992, the contracting officer responded to the Contractors' certified claim, and stated that he did not intend to issue a final decision on that claim. He also advised the Contractors that their payments, as described in Paragraph 361 above, had reduced the amount of unliquidated progress payments for which they are liable to the Government, and further directed them to continue to liquidate progress payments accordingly as they dispose of A-12 Progress Payment Property. In conclusion, he advised the Contractors that he looked "forward to continue working with you to reduce your outstanding liability for the unliquidated progress payments made under the A-12 Contract". Since that time, Plaintiffs have continued, under protest, to make payments to Defendant as a result of certain dispositions of A-12 Progress Payment Property.

363. More than sixty days have passed since the Contractors submitted their certified claim, and no other communication has been received from the contracting officer regarding the Contractors' claim since receipt of the Navy's October 23, 1992 letter. The contracting officer's expressed intention not to issue a decision on the Contractors' claim constitutes a denial of that claim. 41 U.S.C. § 605(c)(5).

364. Defendant's demand that the Contractors repay unliquidated progress payments for each disposition of A-12 Progress Payment Property, and its collection of such amounts, is contrary to the Deferment Agreement, which expressly states that the Navy would not seek repayment of any unliquidated progress payments pending resolution of the Contractors' suit. Similarly, Defendant violated the Deferment Agreement by conditioning approval of any dispositions of A-12 Progress Payment Property upon repayment of unliquidated progress payments. Defendant also failed to consider the "claims by the contractor against the Government" by demanding repayment of unliquidated progress payments, as required by FAR § 32.606(b).

365. The Contractors seek de novo review of the contracting officer's deemed final decision on each of the claims referred to in this Count XX. This Court has jurisdiction over the matters alleged in this Count XX pursuant to section 10(a) of the Contract Disputes Act of 1978 (41 U.S.C. § 609(a), 28 U.S.C. § 1491(a)(2) (1988), as amended by Section

907(b) of the Federal Courts Administration Act of 1992).

WHEREFORE, plaintiffs pray:

A. That this Court enter a judgment holding the A-12 FSED Contract to have been void ab initio, or, in the alternative, voidable; and that the plaintiffs performed under an implied-in-fact cost-reimbursement plus fixed-fee type contract;

B. That this Court enter a judgment reforming the Contract to a cost-reimbursement plus fixed-fee type contract;

C. That this Court enter a judgment holding that the Navy breached the contract;

D. That this Court order the contracting officer to adjust the price of the A-12 FSED Contract upward in accordance with the Contractors' claims for equitable adjustments, and that the Court grant such additional relief as is appropriate, including interest under the Contract Disputes Act from December 31, 1990;

E. That this Court enter a judgment converting the termination for default to a termination for the convenience of the government;

F. That this Court enter a judgment holding that the Navy's demand for return of unliquidated progress payments is of no force and effect by reason of the conversion of the termination for default to a termination for the convenience of the government, and that the Contractors are entitled to

the amount of $1,352,459,644, claimed by the Navy in that demand;

G. That this Court enter a judgment holding that the government's attempt to exercise Lot I was invalid;

H. That Plaintiffs be awarded all of their incurred performance costs plus a reasonable profit, plus settlement expenses;

I. That Plaintiffs be awarded damages for breach of Contract; and

J. That Plaintiffs be awarded their termination for convenience costs, as set forth in their Termination Settlement Proposal and Claim, dated June 26, 1991; and

K. That this Court declare that Defendant acted in violation of the Deferment Agreement, by demanding repayment of unliquidated progress payments upon each disposition of A-12 Progress Payment Property, by conditioning the disposition of A-12 Progress Payment Property upon the immediate repayment of unliquidated progress payments pursuant to subparagraph (d)(5) of the Progress Payments Clause of the A-12 FSED Contract, and by collecting such repayments;

L. That this Court declare that the Navy may not demand repayment of unliquidated progress payments upon each disposition of A-12 Progress Payment property, condition the disposition of A-12 Progress Payment Property upon the immediate repayment of unliquidated progress payments, and collect such repayments;

M. That this Court enter a judgment awarding Plaintiffs damages in the amount of $4,422,674.58, plus interest thereon under the Contracts Disputes Act from August 26, 1992, in satisfaction of Plaintiffs' claims for violation of the Deferment Agreement; and

N. That this Court award plaintiffs such other and further relief as the Court deems just.

Respectfully submitted,

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Dated: February 8, 1993

Dated: February 8, 1993

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Plaintiffs' Motion for Leave to File Second Amended Unclassified Complaint, with Second Amended Unclassified Complaint attached, was served on this 9th day of February, 1993 on the following person by hand delivery.

Mary Mitchelson
Assistant Director
Commercial Litigation Branch
Civil Division
Classification Unit
Todd Building, 2nd Floor
United State Department of Justice
Washington, D.C. 20503

/s/ Thomas F. Burke
Thomas F. Burke

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORPORATION AND GENERAL DYNAMICS CORPORATION	:	No. 91-1204C
Plaintiffs,	:	Filed: March 9, 1993
v.	:	
UNITED STATES OF AMERICA,	:	
Defendant.	:	

ORDER

Defendant requested a stay of our March 5 Order. The Order complained of does not direct the Executive to grant to any individual a security clearance, *Egan* is not applicable. Rather, it directs that two persons who have been deemed trustworthy by the Executive be allowed to aid in plaintiffs' discovery efforts. One of these persons is required by the Air Force to be added to plaintiffs' discovery team. The other is a technical consultant whose need plaintiffs specifically have justified to the court, on the record.

A party to litigation may not control access to discovery by the other parties without the court's approval. Defendant should not use general references to national security to intimidate a court, and it should not be permitted to withhold information without a showing of how national security could be compromised. Defendant has not shown by the affidavit of a former Secretary of the Air Force that state secrets safely can be revealed to 10 trustworthy persons and not 12. Defendant has declined to assist the court in understanding its concerns.

This motion continues a pattern of delay which has frustrated legitimate discovery, and we are not satisfied that defendant is entitled to the relief it seeks. Defendant's motion for a stay of the March 5 Order is DENIED.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS/ GENERAL DYNAMICS Plaintiff,	)	
V.	)	Case No.: 91-1204-C
THE UNITED STATES Defendant.	)	

Courtroom 6, Room 507
U.S. Court of Federal Claims
717 Madison Place, N.W.
Washington, D.C.

Tuesday,
March 23, 1993

The parties met, pursuant to the notice of the Judge, at 10:04 a.m.

BEFORE: HON. ROBERT H. HODGES, JR.
JUDGE

APPEARANCES:

For the Plaintiff:
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For the Defendant:
MARY MITCHELSON, ESQ.
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PROCEEDINGS
THE COURT: Please be seated. Ms. Mitchelson, do you have anything to say in response to these rather cryptic orders?
MS. MITCHELSON: Yes, Your Honor. I have a brief statement.
As you recall, at the time you denied our motion to dismiss Plaintiff's superior knowledge claims, you acknowledged the sensitivity of this area. You also cautioned against a parade through the Pentagon and directed that discovery in this area be extremely narrow.
Subsequently the Plaintiffs propounded very broad interrogatories and other written discovery asking for information from two LO observable programs -- B-2 and F-117. We complained that the discovery requests were so broad as to be irrelevant, particularly because Plaintiffs had not yet then and still have not now identified what is the superior knowledge which is the basis of their allegation.
With your intervention, you were able to narrow the Plaintiff's discovery requests so that they were more narrow and focused, and we have to date identified

about,
23 approximately 60,000 pages of documents responsive to those
24 requests in the program B-2 and F-117A.
25 We understand our obligation in this litigation to

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1 be to respond to properly propounded discovery requests. To
2 the extent those requests have required us to produce
3 information or identify program involving LO observable
4 technology, those responses have been limited to three LO
5 observable program -- A-12, B-2 and F-117A.
6 We do not understand our obligation in this
7 litigation to be to canvass all sources or repositories of
8 LO observable technology in the Government and to disclose
9 to Plaintiffs the results of that search.
10 THE COURT: Well, suppose there were a specific
11 issue that came to your attention? Would you feel the
12 responsibility to decide whether to afford access to
13 Plaintiff's attorneys to that?
14 MS. MITCHELSON: We have a responsibility to
15 respond to properly propounded discovery requests, Your
16 Honor. To the extent there would be a discovery request

which would, to which that particular matter would be a
proper response, we would have an obligation to either
identify it or invoke state secrets.
THE COURT: Suppose the Plaintiff were in a
situation in which it did not know how to propound an
interrogatory that would be on point?
MS. MITCHELSON: That's absolutely inconceivable,
Your Honor, because it is the Plaintiff's theory of superior
knowledge. The Plaintiffs know what failed. They know what

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their failures were in this program. It is incumbent upon
them to identify their failures and identify that
information which they believe the Government possessed but
refused to share with them.
Therefore it is the situation where they have
complete control over the ability to propound
interrogatories related to their claim.
THE COURT: All right, thank you. Mr. Churchill?
MR. CHURCHILL: Thank you, Your Honor. May it
please the Court. Your Honor, we don't have complete
control as Ms. Mitchelson just said, over the
interrogatories that we might propound.

Where the Government impedes even the communication between attorney and client, the attorney is not going to be in a position to propound the discovery that is going to be necessary to find our way through this latest issue on the superior knowledge of discovery. Your Honor, going back to the beginning of this case and the complaint, Ms. Mitchelson says that our discovery was designed as a parade through the Pentagon. Well, in fact, both the allegations of the complaint and the discovery we have propounded has been quite limited and focused. In paragraph [ ] of the original complaint, we alleged that the Government organization sponsoring

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classified programs, including the Navy, and I am quoting now, [

]

The Government denied that allegation as being too vague for them to formulate a meaningful response. In paragraph [ ] on the same page of the original

complaint, we alleged that the Government was aware that the withheld information was vital to the A-12 development and that the contractors did not have available information from other classified program, and had no means to obtain such information on their own.

The access that we are now seeking goes to those allegations, goes to those specific allegations and the discovery we have sought and will continue to seek goes also to those allegations.

It is true that we commenced our discovery with the B-2 and the F-117 programs. Those program are acknowledged program as the Department of Defense calls them.

Since that time, however, we have become aware of other potentially relevant areas that go beyond the B-2 and F-117. In term of the discovery rules, these other matters

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or cells or other program, whatever they may be, are matters that may lead to the discovery of relevant evidence.

These go, as we understand it, to the allegations that we have made in paragraph [ ] and [ ] to [

5
6]
7 These leads that we have tried to pursue in the
8 discovery process, and our efforts just to learn from
our
9 own client what the facts are relating to this dispute,
10 arose out of our efforts to respond to the
Government's
11 discovery, our efforts to draft our own discovery, and
our
12 performance of the basic obligation that we have in
this
13 case, to develop the facts to defend against the
14 Government's termination for default action.
15 The Government here, as elsewhere in the superior
16 knowledge area, has asserted no privilege that would
bar or
17 limit in any way the discovery. The Government has
not made
18 an allegation that the information we are now
seeking is not
19 relevant to this case.
20 We now know from depositions that have been taken
21 as recently as last week that there were [
22
23
24
25]

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1 I would like to quote from one page of the
2 deposition that was taken last week of Richard

Rumpf who
was, I think it is fair to say, the Navy's architect for the
A-12 program.
[
]
So now we have begun to flesh out the allegations
which we made in Paragraph [ ] that [
]
We also note in that same deposition that at least
one of the Government's trial team lawyers in this case has
access to one or more of these cells that we now find
ourselves outside of.
As you know, Your Honor, we have tried to commence
the fact-finding in this area, not by propounding discovery
originally, but simply to learn the facts from our own
client, and we submitted our access package to the
Government within DOD channels for that purpose.

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The Government, after review, including review by
litigation counsel in this case, is denied that access,

and
we find ourselves outside that door without any reason being
given by the United States, and without any privilege having
been asserted.
As a result of that, our Rule 26 rights in
discovery are being frustrated and even more fundamentally,
our right to access to this Court that is guaranteed both by
the Disputes Clause, by the Contracts Disputes Act, and
ultimately by the due process clause, is being denied to us.
What we would like the Court to do here is order
the Government to show cause why we should not be granted
access so that we can pursue this fact-finding and
discovery, if it turns out to be appropriate.
If the Government persists, as it has in other
areas of this superior knowledge discovery in its refusal to
participate in the discovery and to make discovery, then the
mechanisms in Rule 37 of the rules of this Court would
permit the Court to establish as taken, as given, the
factual allegations we have made in Paragraph [ ] Paragraph
[ ] and in the other allegations of our superior knowledge
counts of the complaint.

And I think that is what would be appropriate in this matter.
THE COURT: Thank you. Let me be sure I

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understand the Government's position here being that in essence, what is standing in our way here is the lack of a direct interrogatory from Plaintiff? Is that all you need to move things along?
MS. MITCHELSON: We agree, Your Honor, that we have the obligation to respond to properly propounded interrogatories from the Plaintiffs.
To date, their interrogatories have required our response, to the extent that they have required responses, which might produce material from other LO observable programs, those program have been limited to the three identified.
THE COURT: This seems artificial to me. If we could sit here today and craft a question that would elicit a response that you will either accede to or declare a privilege on, are you telling me that that is all we need to do?
MS. MITCHELSON: Your Honor, I don't mean to

even
19 suggest that there are not outstanding interrogatories to
20 which we must make that consideration. As the Plaintiffs
21 well know how to draft interrogatories to explore the basis
22 of their allegations of the complaint.
23 However, given the way the discovery has gone in
24 this case, we have to date not been required to respond to
25 those. When the times comes that we are required to

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1 respond, yes, we will be required either to reveal the
2 information or to invoke state secrets.
3 The distinction, Your Honor, while it may seem
4 artificial, is important. We do not understand our
5 obligation to be to canvass the entire Government for any
6 program which may be a source or a repository of LO
7 observable information.
8 We do understand our obligation to be to respond
9 to properly propounded interrogatories and other discovery
10 requests which the Plaintiffs believe relate to their
11 allegations in the complaint.
12 We will, have been, and intend to continue to do
13 the latter. We do not see our obligation to be pro forma.
14 THE COURT: You understand though why we are here

today, do you not?
MS. MITCHELSON: To the extent that I have been informed that there has been a request for access to a program which may or may not exist, I cannot confirm or deny, that is my understanding of why we are here, Your Honor.
THE COURT: All right. Now, isn't that a specific issue that we can address whether we have a specific question, interrogatory directed to it?
MS. MITCHELSON: No, Your Honor. A request for access to a program is separate from a request for

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information, specific request for information in this litigation, and our obligation in this litigation is to provide the information pursuant to the rules of this Court.
The fact that there may or may not be another cell which the cell which the Plaintiffs find themselves excluded from is one that is inherent in the nature of special access programs.
We now have had some great deal of experience in the A-12, the B-2 and the F-117A programs. As you know, the programs are created as cells. I think that is an apt term that Mr. Churchill used for specific security reasons.

There are individuals I am confident in the corporations, even of the Plaintiff's corporations who have access to certain cells and not access to other cells. That's the way the world of special access program works, Your Honor.

In this litigation, you have determined that the Plaintiffs may proceed with some discovery, albeit limited or narrow, with regard to their superior knowledge allegations.

We have an obligation to respond to that discovery and we have been doing that, and we will do that.

THE COURT: Well, your understanding of this cell or this program, if it exists, and your understanding of its being the reason we are here today, should suggest to you

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that a decision on that matter at least would enable us to go forward, whether you have a question directed to it or not.

MS. MITCHELSON: Your Honor, we have an obligation to provide information pursuant to properly propounded discovery requests, and . . .

THE COURT: Okay.

MS. MITCHELSON: We would make a decision on privilege at that time, Your Honor.
THE COURT: All right. Thank you. The Defendant in this case, of course, is in a unique position, unique among all Defendants in being able to classify information and control access to information which may be helpful or hurtful to its case.
No one else has that authority and that authority carries responsibility with it. That it controls the program that we have discussed, and also the distribution of information into or from those program, classified or not, acknowledged or not, the result can be an intolerable situation in which Defendant, Defendant's counsel, and Plaintiffs have crucial knowledge, but Plaintiff's counsel do not.
Plaintiff's counsel must be permitted to prosecute Plaintiff's case. It is not acceptable for the Defendant's litigation team to have information which is not available

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to Plaintiff's litigation team.
Attorneys for both sides have been deemed trustworthy by the Executive and none is more

trustworthy
than another. The Supreme Court has established procedures
for protecting national secrets. These procedures provide
standards for all parties to follow, including the Judge.
Such a procedure would eliminate unnecessary
litigation and avoid uncertainty among the parties. Yet
Defendant has chosen not to use this procedure. Therefore
Defendant is admonished that no further interference with
the discovery process will be permitted.
This relates not to the granting of security
clearances, or to issues now before the Federal Circuit.
This addresses Defendant's refusal to disclose information
necessary to Plaintiff's proof of their claims.
If Defendant is not prepared to show that it is
relying on an established privilege as described in the
order filed March 18, we are prepared to direct that certain
information be deemed admitted in accordance with Rule 37.
An order to this effect would be issued no later
than the close of the business on Tuesday, March 30th, 1993.
It is so ordered.
Now, my concern here is among many other

concerns,
24 that, issues in this case, and we discussed this before when
25 we were addressing Count 2, may be created even though they

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1 are sensitive. They may be divined, if you will, by people
2 who are very familiar with this case.
3 It is not hard for someone familiar with this case
4 to infer issues, information, problems, programs that may be
5 highly sensitive. If those parties have no information
6 about how to deal with that, those inferences then, it seem
7 to me, that harm to the national security could result, and
8 it seems to me that it is in the interests of the United
9 States to be sure that people who are involved in this case
10 know what is secret and what's not.
11 I don't understand the reluctance of the United
12 States to be sure that the people who have already been
13 deemed trustworthy in this case are not fully informed about
14 their responsibilities in dealing with these inferences that
15 they could very reasonably have made.
16 So it's not a rule to show cause. I suppose we
17 could put it in that form, but what I want to do is

give you
18 a week, Ms. Mitchelson, to address this problem, the problem
19 we have discussed, and suggest ways to deal with it.
20 If you want to invoke the state secrets doctrine,
21 then we have a procedure for dealing with it, we have a
22 framework. Everybody knows what to do. We can go to look
23 at the cases and see what everybody's rights and
24 responsibilities and duties are.
25 But here we are out in the netherworld of some

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1 sort of new privilege that I believe the United States is
2 trying to craft, that even though short of a state secrets
3 invocation, somehow has greater protection, somehow it can
4 be unilaterally invoked with no review whatsoever.
5 So I have said before I do not want to put the
6 United States in the position of having to invoke the
7 doctrine on anything. I would rather avoid that, but at the
8 same time, that seems to be where we are now. That seems to
9 be all that is left.
10 So unfortunately we can't discuss this as much as
11 we need to, or as openly as we need to, but I am confident
12 that you know what my problem is here, you know

what I want
13 from this.
14 MS. MITCHELSON: Actually, Your Honor, could I ask
15 a few questions for clarification?
16 THE COURT: Yes, you may.
17 MS. MITCHELSON: Thank you. Is your order that we
18 identify and produce information from all LO observable
19 programs in the Government?
20 THE COURT: I don't think that has been solved
21 yet. Has it? I'm not aware of the question that addresses
22 all programs.
23 MS. MITCHELSON: Then is your order limited to the
24 matter which brought us here today?
25 THE COURT: Yes, indeed.

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1 MS. MITCHELSON: Is your order that we disclose
2 the information, or that we grant access to individuals?
3 THE COURT: My order is that you decide whether
4 you want to protect that information through invocation of
5 the state secrets doctrine. If not, there is no reason not
6 to enable the Plaintiff to know whether there is anything
7 there.

MS. MITCHELSON: So we either invoke state secrets or disclose the information.
THE COURT: That seems to be the position you have put the Court in, yes. Is that what you need?
MS. MITCHELSON: I believe so, Your Honor. Thank you.
THE COURT: Good. Anything else, Mr. Churchill?
MR. CHURCHILL: No, Your Honor, just in response to Ms. Mitchelson's question, I would say that it would be put this way, that the Government has either to invoke a privilege, or to remove the impediments to the discovery process.
As a litigant to the case, you are obliged to participate in discovery, to the extent that you don't invoke an applicable privilege.
MS. MITCHELSON: I would just point out that Mr. Churchill has yet to identify a discovery request that he believes would require the revelation of information outside

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of the three LO observable programs I have identified.
Secondly, Your Honor, will you be issuing an order in writing?

THE COURT: This is not sufficient.
MS. MITCHELSON: I just wanted to clarify, Your Honor.
THE COURT: Do you want one in writing?
MS. MITCHELSON: It would be helpful.
THE COURT: All right.
MS. MITCHELSON: Thank you.
THE COURT: I do not understand what you want from Mr. Churchill. We can go over to the skiff and I can sit down and tell you exactly what I want, if that's what you need, Ms. Mitchelson.
MS. MITCHELSON: Well - - -
THE COURT: I don' t know how you can expect under these circumstances which you know well, how you can expect Mr. Churchill to propound an interrogatory.
MS. MITCHELSON: Your Honor, what I'm looking for is clarification of our obligation. I am familiar with my obligations with regard to litigation and responding to discovery.
There seem to be a definition of my obligation here that is broader than that I have encountered in other litigation, and I guess the easiest way for me to explain my

problem is that I don't see a concurrent obligation on the part of the Plaintiffs. If the Defendant somehow has an obligation to identify all of the potentially relevant information even beyond the three programs we have now discussed, then is there a similar obligation on the part of the Plaintiffs and are we equally sharing these broader obligations here?

THE COURT: Do you think the Plaintiff possesses secret information that you don't have?

MS. MITCHELSON: Well, I don't know whether it is secret, Your Honor, but I also don't know that the Plaintiff's attorneys define their obligations as rounding up all potential information, even if we have not asked for it.

THE COURT: Ms. Mitchelson, I'm talking about one thing today. So far as I know, they haven't asked for anything else. I know they asked for this, but I find myself in the difficult situation of feeling that they should have access to broader information so that they can decide, as a matter of their own litigation strategy or whatever they want to decide, what they should do with it, if it exists.

I cannot understand - - I am sure you wouldn't want a situation where your client knew things that you didn't know.

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MS. MITCHELSON: In the world of special access programs, Your Honor, that is inevitable.
THE COURT: But you know this. If you know it, how can you justify their not knowing it.
MS. MITCHELSON: Your Honor, I presume there is information that is about their clients that these attorneys know that they haven't shared with me, and that is the nature of litigation.
I am required to reveal information that is asked for in discovery requests, and we have been doing that, and now you have defined our obligation in a different manner, and I now clearly understand I believe the intent of today's order.
THE COURT: Is there anything else that we should address while we are here?
The discovery group normally meets today, and I suggested to them that if they wanted to, if there is anything to address, we can do that right here. We can go off the record and deal with those matters, if you like, or

stay on the record, for that matter.
Is there anything the discovery group should deal with?
MR. CHURCHILL: Your Honor, we would be pleased to
do that. We would like to go off the record.
THE COURT: All right.

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

* * * * * * *

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,

Plaintiffs,

v.

UNITED STATES OF AMERICA,

Defendant.

* No. 91-1204C

* Filed : March 23, 1993

* * * * * * *

ORDER

Defendant will disclose to plaintiffs' attorneys information currently being withheld, no later than 5:00 p.m. on Tuesday, March 30, 1993. If defendant does not comply with this order, Count IX will be deemed admitted in whole or in part. We could not state fully on the record the need for this order, but lead counsel for defendant is aware of that need.

IT IS SO ORDERED.

/s/ROBERT H. HODGES, JR.
ROBERT H. HODGES, JR.
Judge

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DEFENDANT'S MOTION FOR A PROTECTIVE ORDER

Pursuant to RUSCFC 26(c), defendant respectfully moves for a protective order, upon the grounds that the Executive military state secrets privilege prohibits disclosure of information that the Government has been ordered to produce.

This motion is supported by the attached public declaration of Acting Secretary of the Air Force Michael B. Donley ("Donley Pub. Decl."), App. 1, and by an *in camera, ex parte* declaration by Acting Secretary Donley, filed concurrently with this motion ("*in camera* declaration").

STATEMENT OF FACTS

I. BACKGROUND

In Count IX of their Second Amended Unclassified Complaint, plaintiffs McDonnell Douglas Corporation and General Dynamics Corporation ("plaintiffs") have alleged that the Government breached an implied contractual duty, by not sharing with plaintiffs classified information that was contained in compartmentalized, and even covert or unacknowledged, programs. As the Court is aware, it is the Government's position that no such duty may be implied, as a matter of law, in part because such a duty would render meaningless the careful "special access" restrictions that are necessary to protect this nation's most vital military secrets. *See generally* Executive Order 12,356 sec. 4.2 (April 2, 1982), 3 C.F.R. 166, 174 (1983). Accordingly, the Government moved to dismiss those portions of the complaint that were based upon such an alleged implied contractual duty to share the information.

The Court denied that motion to dismiss. At oral argument on June 10, 1992, the Court stated:

> Now I still don't want to get on with a full scale discovery process that marches through every program in the Pentagon. And I would ask the parties to try to get together and try to come up with a reasonable limitation on this discovery process for Count 9. It is something I would do if I knew how, but I simply don't have enough background

> to know how to limit this. But I do want it limited. I want it limited severely.

App. 9-10. The Court went on to state that it "doesn't take any secret information to determine" whether the Government possessed allegedly superior knowledge, App. 15, and that the denial of the Government's motion to dismiss plaintiffs' "superior knowledge" claims "was not an open-ended sort of ruling, as I read it. It doesn't give me authority, I don't think, to say that [plaintiffs should have] full access to these other programs." App. 16.

Because of the sensitive nature of this area, and because the Court indicated that plaintiffs might pursue their claims utilizing only "severely limited" discovery, to date the Government has attempted to allow this portion of the case to proceed as normally as possible. If discovery and plaintiffs' "superior knowledge" claims were truly to remain "limited," as plaintiffs represented they would, App. 14, 16, there would be some chance that those matters could be resolved in a relatively conventional manner, albeit utilizing secure facilities, classified transcripts, closed proceedings, and other restrictions necessary to safeguard this highly sensitive military information.

II. THE GOVERNMENT'S PRESENT OBLIGATION TO DISCLOSE CERTAIN NATIONAL SECURITY INFORMATION

In February 1993, plaintiffs' attorneys raised with the Court an issue regarding certain highly classified matters, to which plaintiffs' attorneys

desired access. Apparently, the speculations of plaintiffs' attorneys were triggered by general communications with certain employees of the plaintiff corporations.

As a result of plaintiffs attorneys' remarks, the Court initiated its own inquiry, with security personnel of the Department of the Air Force. On or about March 3, 1993, the Court requested and received an *ex parte* oral briefing regarding certain matters, from Air Force security personnel. At a hearing on March 4, 1993, the Court stated that "I think we have a problem," App. 18, but indicated that it was going to continue to explore the matter during the ensuing week. On March 5, 1993, the Court entered an "order," wherein it stated that it would address the matter further, and, "[i]f necessary, additional hearings on the matter will be scheduled." App. 20.

On March 18, 1993, the Court entered an order wherein it stated, *inter alia*, that the Government should not be able to impose a "unilateral restriction on discovery." App. 21. The Court scheduled a hearing for the morning of March 23, 1993.

On March 23, 1993, the Court held the scheduled hearing. The Court inquired of the Government's counsel of record what the Government intended to do about the matter. Counsel responded that the Government understands its litigation obligations to be to respond to properly propounded discovery requests, and noted that no currently due discovery response

requires production or identification of information that would implicate the state secrets privilege. If a discovery request implicated a matter that could not be revealed, counsel further noted, the Government would of course recognize its obligation to invoke the state secrets privilege.

At the hearing on March 23, 1993, and in a subsequent written order on that same day, the Court, *sua sponte*, imposed an obligation upon the Government to disclose to plaintiffs the information to which the Court appeared to allude in its orders dated March 5 and 18, 1993. App. 22. The Court gave the Government one week, until March 30, 1993, to produce such information, or to invoke a valid privilege. If the information was not produced within that one week, the Court stated that it would enter a full or partial finding against the Government, upon Count IX of plaintiffs' Second Amended Unclassified Complaint.

III. THE NEED FOR INVOCATION OF THE STATE SECRETS PRIVILEGE

Because of the threat to national security, the Government cannot confirm or deny the matters to which the Court appears to refer in its March 23, 1993 order, nor can it produce the information it has apparently now been ordered to produce in this litigation.

By necessity, the *in camera* declaration by the Acting Secretary of the Air Force describes the specific nature of the threat to national security posed by disclosure of the matters to which the Court has referred. *See* Donley Pub. Decl. ¶ 12, App. 5.

Invocation of the state secrets privilege here is necessary to protect this nation's unmatched capabilities with regard to the development and use of low observable weapons systems.

As the public declaration of the Acting Secretary of the Air Force explains, the United States is the world leader in the production and operation of low observable technology weapons and aircraft. Low observable weapons systems and aircraft have been used in combat, without the loss of United States' lives or aircraft. No foreign country presently has either the capability to build low observable aircraft or the capability to develop a credible countermeasure to this technology, **[REDACTED]** *See* Donley Pub. Decl. ¶ 13, App. 5-6.

Accordingly, disclosure of the matters to which the Court has referred, whether inadvertent or otherwise, can be expected to cause exceptionally grave damage to national security. Donley. Pub. Decl. ¶¶ 12, 15-16, App. 5-6.

This state secrets privilege invocation is, at this time, limited to the matters directly addressed by the Court's order dated March 23, 1993. Invocation of the state secrets privilege, of course, is not a casual or routine matter, and the extraordinary one-week deadline precluded the Government from addressing anything other than the immediate predicament presented by the Court's March 23, 1993 order. As the Acting Secretary states, however, to the extent that litigation of plaintiffs' "superior knowledge" claims will present an uncontrolled continuing need for release of classified, other-

program special access information related to low observable technology, additional and more comprehensive invocations of the privilege may soon be required. Donley Pub. Decl. ¶ 19, App. 7.

ARGUMENT

I. INVOCATION OF THE STATE SECRETS PRIVILEGE IN THESE CIRCUMSTANCES IS NECESSARY, APPROPRIATE AND JUSTIFIED

As described above, the Government cannot comply with the Court's direction to produce certain information alluded to in the Court's order dated March 23, 1993, without endangering national security. Accordingly, the Acting Secretary of the Air Force has invoked the state secrets privilege.

The method and manner of the Government's invocation of the state secrets privilege in this case is proper. The privilege here is invoked by the Government itself, *United States v. Reynolds*, 345 U.S. 1, 7 (1953); *Ellsberg v. Mitchell*, 709 F.2d 51, 57 (D.C. Cir. 1983), *cert. denied*, 465 U.S. 1038 (1984), and lodged by the head of the agency having control over the matters, after actual, personal consideration. *Reynolds*, 345 U.S. at 7-8; *Ellsberg*, 709 F.2d at 57; *Halkin v. Helms*, 690 F.2d 977, 991 (D.C. Cir. 1982) ("*Halkin II*").

In order for the state secrets privilege to be necessary and valid, there need only be a showing of a "reasonable danger" that national security *might* be damaged. *Reynolds*, 345 U.S. at 10; *Guong v. United States*, 860 F.2d 1063, 1066-67 (Fed. Cir.

1988), *cert. denied*, 490 U.S. 1023 (1989); *In re United States*, 872 F.2d 472, 475 (D.C. Cir.), *cert. dismissed*, 493 U.S. 960 (1989); *Foster v. United States*, 12 Cl. Ct. 492, 494 (1987).

To pose a "reasonable danger" warranting invocation of the privilege, the threat need not be inevitable, nor, significantly, need the threatened disclosure be public. *Northrop Corp. v. McDonnell Douglas Corp.*, 751 F.2d 395, 402 (D.C. Cir. 1984). Even if the parties to the litigation are major "cleared" defense contractors, their counsel have security clearances, and the parties are governed by a protective order regarding classified information, the Government may refuse to disclose its state secrets in litigation. *Northrop*, 751 F.2d at 402 (McDonnell Douglas Corporation and its counsel denied access); *Sigler v. LeVan*, 485 F. Supp. 185, 194 (D. Md. 1980) ("Protective orders cannot prevent inadvertent disclosure nor reduce the damage to the security of the nation which may result."). As long as the information is, as in this case, a state secret, the trustworthiness, or clearance level, of the parties to the litigation is immaterial. *Northrop*, 751 F.2d at 402. This is so because it remains the Government's absolute responsibility to determine with whom it will share particular state secrets. *Halkin v. Helms*, 598 F.2d 1, 9 (D.C. Cir. 1978) ("*Halkin I*") (Government may withhold types of information in one proceeding which were disclosed in another proceeding); *Northrop Corp. v. McDonnell Douglas Corp.*, 751 F.2d 395, 402-03 n.9 (D.C. Cir. 1984) ("[O]ne department's decision to disclose documents it possesses on a given topic should not compel

another department's disclosure when it has decided against such an action.").

In assessing the Government's assertion of the privilege, courts may not, of course, force disclosure of the very thing the privilege is designed to protect. *Reynolds*, 345 U.S. at 8; *Foster*, 12 Cl. Ct. at 495. Accordingly, courts afford "'"utmost deference" to executive assertions of privilege upon grounds of military or diplomatic secrets.'" *Northrop*, 751 F.2d 395, 402 (D.C. Cir. 1985), *quoting Halkin v. Helms*, 598 F.2d 1, 9 (D.C. Cir. 1978) ("*Halkin I*"), *in turn quoting United States v. Nixon*, 418 U.S. 683 (1974). *See also Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 548 (2d Cir. 1991); *In re United States*, 872 F.2d at 475. This judicial deference is grounded in the "willingness [of the courts] to credit [even] relatively speculative projections of adverse consequences" to national security. *Ellsberg*, 709 F.2d at 58 n.35.[1]

Consistent with these principles, the Acting Secretary of the Air Force has properly determined that invocation of the privilege in this case is most appropriately accomplished through a public declaration, and a more detailed *in camera*

[1] This judicial deference ultimately arises out of the constitutional separation-of-powers underpinnings of the state secrets privilege itself. *See United States v. Nixon*, 418 U.S. 683, 705-06 (1974); *Salisbury v. United States*, 690 F.2d 966, 976 n.4 (D.C. Cir. 1982); *Black v. Sheraton Corp.*, 564 F.2d 531, 541 (D.C. Cir. 1977). *Cf.* 8 C. Wright & A. Miller, *Federal Practice and Procedure* § 2019 (1970) (noting a "constitutional privilege to refuse to disclose whatever the executive chooses to keep secret").

declaration, filed simultaneously with this motion. Those declarations conclusively establish the harm to national security that would be caused by disclosure of the privileged information, and provide a more than adequate basis for the Court to confirm the legitimacy of the privilege here. *Zuckerbraun*, 935 F.2d at 548; *Halkin II*, 690 F.2d at 992; *Xerox v. United States*, 12 Cl. Ct. 93, 95 (1987) (presumption that declarations are prepared faithfully and properly); *American Tel. & Tel. v. United States*, 4 Cl. Ct. 157, 161 (1983) (no requirement of *in camera* showing for invocation of privilege). *See also Reynolds*, 345 U.S. at 10 (no requirement of *in camera* showing; court may take judicial notice of other evidence regarding sensitivity of matters); *Ellsberg*, 709 F.2d at 61.

Plaintiffs' counsel may not be afforded access to the *in camera* declaration, in these circumstances. *E.g.*, *Ellsberg*, 709 F.2d at 61 ("It is well settled that a trial judge . . . should not permit [plaintiffs'] counsel to participate in an *in camera* examination of putatively privileged material."); *Salisbury v. United States*, 690 F.2d 966, 973, 977 (D.C. Cir. 1982); *Halkin I*, 598 F.2d at 7; *Jabara v. Webster*, 691 F.2d 272, 274 (6th Cir. 1982), *cert. denied*, 464 U.S. 863 (1983). This is not altered by the fact that plaintiffs' counsel have security clearances. *Foster*, 12 Cl. Ct. at 496.

The above authorities, and the public and *in camera* declarations filed with this motion, conclusively demonstrate that the Government has

properly, and necessarily, invoked the state secrets privilege in this case.

II. THE STATE SECRETS PRIVILEGE IS ABSOLUTE

It is well-established, of course, that the state secrets privilege is absolute, and no showing of need can overcome the privilege. *E.g.*, *United States v. Reynolds*, 345 U.S. 1, 11 (1953); *Langenegger v. United States*, 756 F.2d 1565, 1569 (Fed. Cir.), *cert. denied*, 474 U.S. 824 (1985); *In re United States*, 872 F.2d 472, 475 (D.C. Cir.), *cert. dismissed*, 493 U.S. 960 (1989); *Northrop Corp. v. McDonnell Douglas Corp.*, 751 F.2d 395, 399-400 (D.C. Cir. 1984); *American Tel. & Tel. v. United States*, 4 Cl. Ct. 147, 161 (1983). Upon invocation of the privilege, the information may not be disclosed. *E.g.*, *Fitzgerald v. Penthouse Int'l, Ltd.*, 776 F.2d 1236, 1240 (4th Cir. 1985); *Halkin v. Helms*, 690 F.2d 977, 990 (D.C. Cir. 1982) ("Halkin II"); *Ellsberg v. Mitchell*, 709 F.2d 51, 57 (D.C. Cir. 1983), *cert. denied*, 465 U.S. 1038 (1984); *Foster v. United States*, 12 Cl. Ct. 492, 494 (1987).

The invocation of the state secrets privilege is necessary and proper in these circumstances. Accordingly, the Court should enter a protective order, relieving the Government from the obligation to disclose state secrets that would endanger national security.

CONCLUSION

For the reasons stated above, we respectfully request a protective order relieving the Government

of any obligation to disclose the state secrets that are the apparent subject of the Court's March 23, 1993 order.

Respectfully submitted,

STUART E. SCHIFFER
Acting Assistant
Attorney General

/s/DAVID M. COHEN
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Director

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March 30, 1993

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DECLARATION OF THE ACTING SECRETARY OF THE AIR FORCE MICHAEL B. DONLEY

I, Michael B. Donley, declare:

1. I am the Acting Secretary of the Air Force. As such, I am currently the head of the Department of the Air Force. I am responsible for, and have the authority necessary to conduct, all affairs of the Department of the Air Force. Subject to the authority, direction and control of the Department of Defense, I am also presently responsible for the formulation of policies and programs by the Department of the Air Force that are fully consistent with national security objectives and policies established by the President and the Secretary of Defense.

2. In my capacity as chief executive officer of the Air Force, I possess original classification authority, and am authorized by the President under Executive Order 12356 to determine the proper classification of information, and, in conjunction with appropriate individuals within the Department of Defense, to create compartmentalized, or "special access," programs in order to further safeguard against the unauthorized disclosure of militarily sensitive information.

3. The purpose of this public declaration is to invoke the military and state secrets privilege, in order to protect the national security of the United States. Because a more detailed public description of certain matters for the record is not possible, I am also submitting an *in camera* declaration to the Court, which provides a further explanation of this invocation of the military and state secrets privilege.

4. The statements in this declaration are based upon my personal review and consideration of these matters. Specifically, among other things, I have considered the recent orders of the Court, including its order dated March 23, 1993, and I have reviewed the nature of the subject information, described in more detail in my *in camera* declaration.

A. General Classification Procedures, And Restrictions Upon Access To National Security Information

5. Generally, classification of information within the Department of Defense is done in accordance with Executive Order ("E.O.") 12356, which prescribes a uniform system for classifying,

declassifying, and safeguarding national security information. Executive Order 12356 (April 2, 1982), 3 C.F.R. 166 (1983), *reprinted in* 50 U.S.C.A., at 208 (1991); and Presidential Order of May 7, 1982, 3 C.F.R. 257 (1983), *reprinted in* 50 U.S.C.A., at 217 (1991). E.O. 12356 authorizes three levels of classified information: top secret, secret, and confidential.

6. Pursuant to Department of Defense ("DOD") Directive 5200.1, originally issued in 1982, it was (and is) the policy of the Department of Defense to use traditional classification categories wherever possible. In addition, however, an agency head (in this case the Secretary of the Air Force, with the concurrence of the Deputy Secretary of Defense) may designate a program as a "special access program" (discussed below) when he determines that the information is of such sensitivity and importance that the normal security procedures authorized for a secret or top secret program are not sufficient to limit access appropriately. DOD Directive 5200.1, § 159.120, 47 Fed. Reg. 38,284, 38,316 (1982) (codified as revised at 32 C.F.R. § 159a.80 (1991)).

7. When necessary, such additional protection for classified information is available to programs designated as "special access programs." *See* 32 C.F.R. § 2001.45 (1987) (criteria for special access program status). Special access program status is intended to protect those specially sensitive programs that cannot be adequately protected by the level of security and access controls afforded secret or top secret non-special access programs. *See* 32

C.F.R. § 2001.45. The "special access" designation is reserved for particularly sensitive classified programs in order to control the access, distribution, and protection of information pertaining to these special access programs.

8. An individual must possess a security clearance of secret or top secret as a prerequisite for access to a special access program. Possession of a security clearance is only the first step toward approval for access to a special access program. These programs are characterized in part by an additional adjudication, to a more stringent standard than the adjudication for a security clearance. *See* DOD Directive 5200.2-R, 52 Fed. Reg. 11,219 (1987) (codified at 32 C.F.R. § 154) (outlining security review of personnel in special access programs).

9. Special access programs also impose "need to know" and access controls beyond those normally required by DOD regulations for access to confidential, secret, and top secret information. Access to information within a special access program is granted only to those persons who are essential to the successful completion of the program, and who meet all stipulated security requirements. Other more stringent security measures in effect in special access programs are enhanced physical, technical, communications, computer, operations, and information security.

10. Special access programs may be acknowledged (overt) or unacknowledged (covert) in nature. The mere existence of an unacknowledged program is classified within the boundaries of the

special access program. That is, one must be approved for access before one may know that the program exists at all.

11. A further aspect of special access programs is that they are "compartmented." *See* Section 4.2 of E.O. 12356. That is, the information in the program is, in effect, walled off from other classified information and programs. For example, it is not uncommon that individuals, either Government or contractor personnel, may work in a secure facility that contains more than one special access program. An individual may have access to one special access program while his colleagues have access to different special access programs. Despite the fact that the individuals are professional colleagues, that they possess the requisite security clearances, and they work in the same secure facility, such individuals are still prohibited, absent being given access to another program, to share special access information across program boundaries. The purpose of this requirement is that in the event of a breach of security the potential damage is limited to that one special access program. In effect, the "compartmented" nature of a special access program works as a damage control brake, in the event of an unauthorized disclosure.

B. The National Security Interests At Stake

12. The specific reasons why discrete disclosures would endanger national security are, necessarily, explained in more detail in the accompanying *in camera* declaration. Generally, however, the unauthorized disclosure of low

observable technology could be expected to cause exceptionally grave damage to national security.

13. The United States is the world leader in the production and operation of low observable technology weapons and aircraft. Low observable weapons systems and aircraft have been used in combat, without the loss of United States' life or aircraft. We believe that no foreign country presently has either the capability to build low observable aircraft or the capability to develop a credible countermeasure to this technology. The United States has a very limited capability to counter this technology, should it be developed and used against us by a foreign country. Accordingly, inadvertent, unauthorized disclosure of the information that is described in more detail in my *in camera* declaration could severely jeopardize national security.

C. The Information At Issue

14. The matters to which the Court appears to refer in its orders dated March 5, 1993, March 18, 1993, and March 23, 1993 cannot be commented upon further in a public declaration, and my determinations in that regard are described in more detail in the *in camera* declaration.

D. My Determinations Regarding National Security And The Military and State Secrets Privilege

15. The Air Force cannot confirm or deny the existence of the information apparently sought

by plaintiffs, and referenced in the orders of the court.

16. Even if the parties and Court attempted to take all conceivable precautions, I believe that there is a substantial risk that national security would be threatened by disclosure of these matters, for purposes of this litigation. Accordingly, I view my responsibility to protect the national security as requiring that I invoke the extraordinary measure of asserting the military and state secrets privilege.

17. I have personally determined that the privilege claims which I now assert in this declaration are appropriate under the circumstances.

18. For these reasons, and the reasons explained in more detail in the accompanying *in camera* declaration, I invoke the military and state secrets privilege, and deny access to such information in this lawsuit.

19. This present assertion is limited to the matters that appear to be referenced in the Court's orders dated March 5, 1993, March 18, 1993, and March 23, 1993. I am informed, however, of the nature of plaintiffs' allegations that the Government had a duty to share information relating to low observable, stealth technology, notwithstanding the fact that such information might be contained in classified, top secret, special access programs. I understand those allegations generally to be referred to as plaintiffs' "superior knowledge" claims. To the extent that litigation of those "superior knowledge" claims will present a continuing need for release of classified, special access information related to low

observable technology, I will continue to view my responsibility to protect the national security as requiring invocation of the military and state secrets privilege.

20. I declare under penalty of perjury that the forgoing statements are true and correct to the best of my knowledge, information and belief.

/s/ Michael B. Donley
Michael B. Donley
Acting Secretary of the Air Force

Executed this 30th day of March, 1993.

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C
v.	)	Filed: April 16, 1993
UNITED STATES OF AMERICA,	)	
Defendant.	)	

ORDER

Defendant has not responded to an issue which concerns this court. Secretary Donley referred to a substantial risk that national security would be threatened by disclosure of certain information for purposes of this litigation. Defendant's litigation team obtained such information and defendant's attorneys have used such information for tactical purposes involving the merits of plaintiffs' superior knowledge claim.

The Federal Circuit is deciding whether plaintiffs must withhold such information from their attorneys because defendant has invoked the state secrets doctrine. However, it is our responsibility to

ensure that one party does not obtain improper advantage over the other during discovery or trial. Whether defendant may continue to use this information for litigation advantage has not been presented to the Federal Circuit.

We expect assurances from defendant that such use of sensitive information for tactical advantage will not recur.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

NOTE: Pursuant to Fed. Cir. R. 47.8, this order is not citable as precedent. It is a public record.

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

MISCELLANEOUS NO. 370

IN RE UNITED STATES,

Petitioner.

ON PETITION FOR WRIT OF MANDAMUS

Before ARCHER, Circuit Judge, FRIEDMAN, Senior Circuit Judge, and MICHEL, Circuit Judge.

MICHEL, Circuit Judge.

ORDER

The United States petitions for a writ of mandamus commanding the United States Court of Federal Claims to vacate its March 5, 1993 order that the Acting Secretary of the Air Force must grant access to two additional individuals representing McDonnell Douglas Corporation and General Dynamics Corporation to two classified and compartmented Air Force programs. The United States argues that the court exceeded its lawful authority in ordering increased access to these programs because as a matter of law such access decisions are committed exclusively to the Chief Executive or his delegatee, here the Secretary of the

Air Force. McDonnell Douglas and General Dynamics oppose.[1] We grant the writ.

BACKGROUND

This mandamus petition arises from a lawsuit by McDonnell Douglas and General Dynamics against the United States because of the Department of the Navy's termination for default of their contract to produce a stealth attack aircraft called A-12 for basing on aircraft carriers. McDonnell Douglas and General Dynamics claim, *inter alia*, that the United States breached an implied duty to share with plaintiffs "superior knowledge" about problems in producing stealth aircraft, and their solution, that were discovered in earlier production of the B-2 and A-117A stealth aircraft by other manufacturers. After the court denied the government's motion to dismiss, McDonnell Douglas and General Dynamics sought broad discovery from the Department of the Air Force concerning the B-2 and A-117A programs. Portions of these programs were classified as "Special Access Programs," a more restrictive classification of national security information than a secret or top secret classification. McDonnell Douglas and General Dynamics requested that 17 persons be granted access to review information in the two programs. The court passed this request on to the Secretary via government counsel. The court also allowed the government to respond. In its

[1] The United States moves for leave to file a reply, with reply attached. McDonnell Douglas and General Dynamics move for leave to file a sur-reply, with sur-reply attached. We grant the motions.

response, the United States included a declaration from Donald B. Rice, then secretary of the Air Force. The Secretary determined that not more than 10 individuals shall be granted access. In the November 20, 1992 declaration, the Secretary explained his decision:

> 4. . . . I have designated portions of the B-2 and F-117A programs as "Special Access Programs" under [Executive Order] 12356. The "Special Access" designation is reserved for particularly sensitive classified programs in order to *further control the access*, distribution, and protection of information pertaining to it. Special Access Programs impose "need to know" and access controls *beyond those normally required* by Department of Defense regulations for access to Confidential, Secret, or Top Secret information. Access to information within a Special Access Program will be granted only to those persons who are essential to the successful completion of the program, or who are required for proper coordination and oversight, and who meet all stipulated personnel security requirements. . . .
>
> 5. To comply with the Executive Order 12356 *requirement to limit access to the greatest extent possible*, I have determined the following: a) not more

> than 10 individuals (*including counsel, consultants, or engineers*) representing the plaintiffs, are hereby authorized access to the Secret/Special Access level of the B-2 and F-117A programs; b) not more than 4 of those 10 individuals are hereby authorized access to the Top Secret/Special Access level of the B-2 and F-117A programs. Each individual must meet all clearance eligibility criteria in the programs' security guides.

(Emphasis added.)

The Secretary of the Air Force detailed the dangers associated with unauthorized disclosures of the technological information, stating, *inter alia*, that it would "weaken our country's ability to defend itself," and that such disclosures also "could place at risk our aircraft and the lives of the crews of those aircraft." The Secretary concluded:

> 9. It is my judgment, after personal consideration of the matter, that the national security information at issue in this litigation, and described herein, *must be limited and strictly controlled in the interests of the national security* of the United States. The limited access authorized in paragraph 5 above is consistent with the strict limitations that are applied to government employees for access to this national security information.

(Emphasis added.)

In an order dated December 2, 1992, the Court of Federal Claims directed McDonnell Douglas and General Dynamics to submit the names of 10 persons to the Air Force for access to the programs as granted by the Secretary. They were identified and given actual access. They included technical specialists and attorneys.

On February 12, 1993, McDonnell Douglas and General Dynamics moved that two additional persons be granted access by the Secretary to the programs. McDonnell Douglas and General Dynamics noted that the two additional persons included a consultant to better coordinate the technical specialists and a security officer that from the start the Air Force rules had required. The United States responded by citing the Secretary of the Air Force's decision set forth in his declaration that limited access to "not more than 10 individuals (*including* counsel, *consultants*, or engineers)." (Emphasis added.) In an order dated March 1, 1993, the Court of Federal Claims directed attorneys for the United States to "request" that the Acting Secretary of the Air Force reconsider the Air Force's denial of access for the additional persons. At the same time, however, the Court of Federal Claims rejected the United States' argument that the Secretary of the Air Force's decision on access was judicially unreviewable, but without citing any authority or explaining its reasons beyond its "responsibility for supervising discovery." The Court of Federal Claims ordered that "[i]f the Air Force

determines not to accommodate this limited *request* [to reconsider], defendant will present at the March 4 hearing the Air Force official who can explain fully the rationale for that decision." (Emphasis added.) At the March 4 hearing, the United States stated that the Acting Secretary of the Air Force had declined to modify the previous determination of Secretary Rice and that an officer, if produced, could not testify with "any more depth than the Secretary's [declaration]" about the basis for the denial of access to more than 10 individuals.

On March 5, 1993, the Court of Federal Claims made the following findings:

> 1. Plaintiffs have demonstrated the need for two additional persons with access to the Air Force programs, one of whom has been required by the Air Force itself; and
>
> 2. Defendant has provided the court *no reasons other than "national security"* for not admitting two additional people to the Air Force programs; and
>
> 3. No reasons appear to the court why 10 trustworthy persons with security clearances present *no threat* to national security while 12 trustworthy persons with security clearances might.

(Emphasis added.)

The Court of Federal Claims then embarked on a new course. In contrast to its earlier orders

"requesting" that greater access be granted by the Acting Secretary, the court now reviewed and reversed Secretary Rice's access decision that had been confirmed by the Acting Secretary. The court *ordered* that the Air Force immediately "arrange for two persons representing the plaintiffs to be admitted to the Air Force programs in issue." As before, the court cited no source of legal authority for a judge to review or countermand a decision under the Executive Order by a service secretary limiting access to classified, compartmented documents and data. The Court of Federal Claims denied the United States' motion for a stay on March 9, 1993. The United States petitioned this court for a writ of mandamus and on March 12, 1993, we stayed the Court of Federal Claims' order pending our disposition of this mandamus petition.

THE ISSUE

The dispositive legal issue governing this petition for writ of mandamus is very narrow. The issue is not whether the trial court can control the scope of discovery: That is not contested here. Nor is it whether the government may lawfully withhold classified national security information and documents: That, too, is uncontested, as the government has provided access to all documents in the two programs, at least to 10 individuals. Instead, the issue is simply whether the Court of Federal Claims has authority to review and reverse a determination by the Secretary of the Air Force, under Executive Order 12356, regarding the number

of persons to whom he shall grant access for Special Access Programs.

DISCUSSION

I. THE GOVERNMENT'S ARGUMENT

At the outset, we emphasize that the United States is not asserting the "state secrets privilege to protect national security." *See United States v. Reynolds*, 345 U.S. 1 (1953). Additionally, the United States does not argue that it has determined that the particular persons sought to be added to the group reviewing the programs are untrustworthy or otherwise not eligible for security clearances.[2]

What the United States does argue is that the Court of Federal Claims both breached the constitutionally required separation of powers and exceeded its lawful authority by countermanding an access decision of a service secretary, as the President's delegatee, under the Executive Order. In support of this petition, the United States makes the following arguments:

- "control of access to classified information is exclusively committed to the sole exercise of judgment by the Executive Branch"

- that this exercise of judgment "encompasses the Executive's compelling interest in limiting access to that classified information"

[2] McDonnell Douglas and General Dynamics state that the two additional persons already have security clearances at high enough levels, although of course they do not presently have grants of access to the two Special Access Programs.

· and because Executive Branch decisions to grant or deny security clearances "may not be second-guessed by the courts," the courts "may not direct the Executive to grant or deny access to classified, compartmentalized information."

The United States relies primarily on *Department of Navy v. Egan*, 484 U.S. 518 (1988), and its progeny to support its proposition that "control of access to classified information is exclusively committed to the sole exercise of judgment by the Executive Branch." In *Egan*, the Supreme Court held that the Merit Systems Protection Board (Board) lacked authority to review a denial of a security clearance whereby a federal employee was automatically removed from his temporary position at a nuclear submarine base after his application for a required security clearance was denied. The Supreme Court stated that "the grant of security clearance to a particular employee [is] a sensitive and inherently discretionary judgment call [and] is committed by law to the appropriate agency of the Executive Branch." *Egan*, 484 U. S. at 526-27. The Supreme Court noted that, *absent a controlling statute*, the Executive has exclusive authority to "classify and *control access to information* bearing on national security *and* to determine whether *an individual* is sufficiently trustworthy to occupy a position . . . that will give that person access to such information" (emphasis added) and that such authority originates in the United States Constitution, Art. II, §2. Section 2 provides that the "President shall be the Commander in Chief of the Army and Navy of the United States." The Supreme

Court observed, even more broadly, that "*unless Congress specifically has provided otherwise*, courts have traditionally been reluctant to intrude upon the authority of the Executive in military and national security affairs." *Egan*, 484 U.S. at 530 (emphasis added). Because Congress did not specifically empower the Board to review the Executive's decision to deny a security clearance, the Supreme Court held that the Executive's decision was not reviewable by the Board. *Egan*, 484 U.S. at 530-32.

II. THE CONTRACTOR'S RESPONSE

McDonnell Douglas and General Dynamics argue that *Egan* and derivative cases do not apply because *Egan* stands only for the "limited proposition" that absent a statute, the judiciary will not review an Executive decision concerning *an individual's* poor character or conduct in the context of granting or denying a security clearance. McDonnell Douglas and General Dynamics argue that the present case is instead controlled exclusively by the general authority of the Court of Federal Claims to manage discovery. Presumably, this argument is based on the authority granted to the judge in the Rules of the Court of Federal Claims. McDonnell Douglas and General Dynamics cite, as explanatory authority on such rule-based discovery powers, *inter alia*, *Reynolds*, 345 U.S. 1, *Webster v. Doe*, 486 U.S. 592 (1988), *In re United States*, 872 F.2d 472 (D.C. Cir.), *cert. dismissed*, 493 U.S. 960 (1989), and *In re United States Department of Defense*, 848 F.2d 232 (D.C. Cir. 1988). McDonnell Douglas and General Dynamics assert that even in

cases involving national security documents and information, a trial court does not lose all authority to review Executive determinations affecting the scope of what may be discovered. McDonnell Douglas and General Dynamics conclude that mandamus must therefore be denied in any case involving the discretionary authority of the Court of Federal Claims to manage any aspect of the conduct of discovery.

The problem with this argument, however, is its premise. The issue in this case does not involve the trial court's discretionary authority to manage discovery, usually by deciding what is discoverable. That authority is clear. *See Florsheim Shoe Co. v. United States*, 744 F.2d 787, 797 (Fed. Cir. 1984) (stating that "[q]uestions of the scope and conduct of discovery are, of course, committed to the discretion of the trial court"). Nor does the government question this authority. Rather, the issue is limited to the authority of the Court of Federal Claims to review the Secretary's determination under Executive Order 12356 to limit the number of persons who may access two Special Access Programs. The Secretary's determination does not limit *what* is discoverable in this case, but only *how many individuals* may have access to admittedly discoverable information.

Reynolds and the related cases relied on by McDonnell Douglas and General Dynamics involve invocation of the state Secrets Privilege to *prevent* discovery of certain documents and are therefore inapposite. In fact, they only highlight that here the

United States is *not* so limiting the scope of discovery. Assertion of the State Secrets Privilege limits what information may be discovered by the United States' party opponent. Here, by not invoking the privilege, and by allowing discovery of all the requested materials, at least by 10 individuals, the United States clearly does not restrict *what* may be inspected.[3] At most, the Air Force decision affects only the pace of discovery, and that only marginally. To the extent plaintiffs impliedly argue that the quality of their review is diminished by the absence of a consultant, the Air Force answers that they could have made the consultant one of their 10 persons designated for access, as Secretary Rice's declaration explicitly required.

In any event, the State Secrets Privilege cases show, at a minimum, that the trial court does indeed lose authority over discovery of national security documents. The only exercise of authority that does remain is limited to an *in camera* review of the documents *by the judge* for the purpose of insuring that the privilege has been properly invoked. Even

[3] For similar reasons, we do not find applicable cases involving motions to dismiss that were based, *inter alia*, on the government's assertion that without dismissal classified documents could be disclosed. *See, e.g., Webster*, 486 U.S. 592; *In re United States*, 872 F.2d 472. Those cases relied on *Reynolds* and discussed the ability of a trial court to determine, to a limited degree, whether discovery of classified documents was permissible as an alternative to dismissing the case because adequate precautions could be instituted to protect state secrets from public disclosure.

then, that review may occur only if the Secretary's declaration is seen as insufficient. In either case, the only issue for the judge is whether the privilege has been properly invoked. Where the privilege is properly invoked, the government's party opponent is not allowed to discover the materials. Indeed, in some cases, the threat to national security may be so great that "the court should not jeopardize the security which the privilege is meant to protect by insisting upon an examination of the evidence, even by the judge alone, in chambers." *Reynolds*, 345 U.S. at 10. Even if the case must therefore be dismissed, discovery is nevertheless blocked.

Similarly, we conclude that cases relied upon by McDonnell Douglas and General Dynamics involving the Freedom of Information Act (FOIA) are not applicable in deciding whether the Secretary of the Air Force's determination under Executive Order 12356 is judicially reviewable. In those cases, Congress specifically provided for limited judicial review of the Executive's determination by statute. No such statute is applicable to the Secretary's access determinations under Executive Order 12356.

For example, McDonnell Douglas and General Dynamics cite *Lesar v. United States Department of Defense*, 636 F.2d 472 (D.C. Cir. 1980), as support for its argument that a trial court has discretion to examine the basis for a national security classification. Under FOIA, however, the government may only claim an "exemption" for documents by establishing that the documents are: (1) related to national defense or foreign policy, (2)

authorized to be kept secret under criteria in an Executive Order, and (3) properly classified. 5 U.S.C. § 552; *see, e.g., Lesar*, 636 F.2d at 481. Thus, the FOIA statute specifically places the burden on the government to sustain its action and impliedly authorizes the district court to review the documents, usually *in camera*, simply to determine whether they are in fact properly classified and therefore exempt. That statutory provision in FOIA cases destroys their relevance to this case, where there is no such statute. Moreover, plaintiffs do not challenge the validity of the classifications here. Nor could they.

III. ANALYSIS OF EGAN AND SEPARATION OF POWERS CASES

A. Egan

Having concluded that the cases relied upon by McDonnell Douglas and General Dynamics are inapposite and that *Egan* is not distinguishable, two questions arise: (1) whether a decision to deny access to a particular individual is legally any different from a decision under the very same Executive Order to deny access to any additional individuals and (2) whether *Egan* requires a conclusion that the Secretary's determination under Executive Order 12356 is no more reviewable by the judiciary than by the MSPB. We answer the first question negatively and the second question affirmatively.

First, the Executive's decision to deny a particular individual a security clearance is functionally identical to the Secretary's decision here to deny additional persons access to the classified

Special Access Programs. In both instances, the decision is based essentially on the same factors. For example, the deciding official must weigh the importance of the information, the harm from disclosure, the acceptable level of risk to national security, and the potential for leaks or disclosures, including purely inadvertent ones. The only distinguishing factor between an individual's security clearance determination and the determination made in this case is that here the Secretary is not evaluating an individual's credibility or trustworthiness. This distinction, however, is not material, and hence does not remove our decision from the principle for which *Egan* stands. Indeed, that is why *Egan* discussed "access to information" as well as "an individual's" trustworthiness.

As noted above, the Supreme Court stated that "the grant of security clearance to a particular employee [is] a sensitive and inherently discretionary judgment call." *Egan*, 484 U. S. at 527. Noting that "[p]redictive judgment of this kind must be made by those with the necessary expertise in protecting classified information," the Supreme Court concluded that "the *protection of classified information* must be committed to the broad *discretion of the agency responsible*, and this must *include* broad discretion to determine who may have access to it." *Egan*, 484 U.S. at 529 (emphasis added). By speaking more broadly of "protection of classified information, and that this would "include" individual clearance decisions, the Court made clear that what was committed exclusively to the

Executive was *more* than just whether an individual could be denied a security clearance.

Moreover, the Court noted that the general standard for security clearance determinations, *i.e.*, whether grant of a security clearance would be "clearly consistent with the interest of national security," presumes no access in close cases and requires that only if the responsible official concludes that the access would be without significant risk may it be granted. The court emphasized that reaching such a predictive judgment is "an inexact science at best." *Egan*, 484 U.S. at 528-29. The Supreme Court concluded therefore that "it is not reasonably possible for an *outside non-expert body* to review the substance of such a judgment and to decide whether the agency should have been able to make the necessary affirmative prediction *with confidence*." *Egan*, 484 U. S. at 527 (emphasis added). According to *Egan*, the expertise required for this type of determination, reinforced by the constitutional separation of powers, makes such a "predictive judgment" one exclusively for the Executive and therefore not reviewable by the Board. While, under *Egan*, such a determination arguably might not be exclusively for the Executive *if* Congress had enacted a statute allowing for some level of outside review and if that statute were held constitutionally permissible under separation of powers, no such issues are presented here for no statute even arguably applies. The decision here was based solely on the Secretary's authority under the Executive Order, which in turn derives exclusively from the

constitutional grant of power to the Executive to command the military and conduct foreign affairs.

Here, the Secretary of the Air Force's determination that not more than 10 individuals shall have access to the programs reflected the constraints imposed on him as the responsible official under Executive Order 12356. As to Special Access Programs, section 5.3 of Executive Order 12356 provides:

> Agencies that originate or handle classified information shall: . . .
>
> [c] establish procedures to prevent unnecessary access to classified information, including procedures that [i] require that a demonstrable need for access to classified information is established before initiating administrative clearance procedures, and [ii] ensure that *the number of persons granted access* to classified information is *limited to the minimum* consistent with operational and security requirements . . . .

(Emphasis added.)

We conclude that the Secretary of the Air Force's determination that not more than 10 individuals should have access to the programs at issue herein is exactly the same kind of "predictive judgment" that was at issue in *Egan*. *Egan*, 484 U.S. at 529. Just as "predictive judgment" was determined in *Egan* to be not reviewable by the non-

expert Board, we conclude that the Secretary's predictive judgment in this case is not reviewable by the non-expert Court of Federal Claims (or the non-expert Court of Appeals for the Federal Circuit, for that matter). Moreover, the Executive Order specifically directs the Secretary to limit access as much as possible. It makes him solely responsible for protecting the national security data. Implicit in *Egan* was the notion that because both "responsibility" and "expertise" reside exclusively in the service secretary, *no* "outside" review was authorized by law, at least absent a clear statutory command to the contrary. That was so even as between agencies *within* the Executive Branch: the Navy and the Board. *A fortiori*, it is so as between different Branches.

The findings made by the Court of Federal Claims in this case clearly indicate the wisdom of precluding review by a non-responsible, non-expert, outside body. The judge found, for example, that "[d]efendant has provided the court no reasons other than 'national security' for not admitting two additional people to the Air Force programs." A cursory review of the secretary's declaration, however, indicates that the government has not merely cited "national security." Rather, the Secretary recited specifically what harm would befall United States National security and the safety of its armed forces personnel. For example, in addition to the expressed danger to U.S. air crews, the Secretary pointed out that if our stealth technology be compromised, "[t]he United States has very limited

capability to counter this technology, should it be developed and used against us by a foreign country."

Similarly, the judge found that "[n]o reasons appear to the court why 10 trustworthy persons with security clearances present *no threat* to national security while 12 trustworthy persons with security clearances might." (Emphasis added.) This finding also misreads the Secretary's declaration. By allowing only 10 individuals access to the programs, the Secretary did not determine that 10 individuals posed "no threat" to national security. Rather, he merely determined that disclosure to 10 people was the maximum tolerable risk to national security. That he gave "no reasons" is entirely unsurprising since to do so would require extensive discussion of highly technical stealth data and vulnerability assessments which, in addition to being beyond the competence of generalist judges, are themselves extremely highly classified.

Moreover, just as there was no controlling statute in *Egan* allowing for Board review, there is no controlling statute in this case allowing for Court of Federal Claims review. The only law applicable here is Executive Order 12356. That Executive Order is in the "series of Executive Orders" applicable in *Egan*, which "have sought to protect sensitive information and to ensure its proper classification throughout the Executive Branch." *Egan*, 484 U.S. at 528. Executive Order 12356 authorizes service secretaries to grant access; it gives no such authority to judges. Thus, we conclude that the Court of Federal Claims does not have any lawful

authority, statutory or otherwise, to review and reverse the Secretary of the Air Force's determination as to the number of persons given access to the two Special Access Programs here, both classified under Executive Order 12356.

B. Separation of Powers

General case law concerning the separation of powers doctrine further supports our conclusion. *See, e.g., New York v. United States*, 112 S. Ct. 2408, 2431 (1992) ("The Constitution's division of power among the three Branches is violated where one Branch invades the territory of another."). *See also Lujan v. Defenders of Wildlife*, 112 S. Ct. 2130, 2136 (1992) ("[T]he Constitution's central mechanism of separation of powers depends largely upon common understanding of what activities are appropriate to legislatures, to executives, and to courts.").

As noted above, the Executive's "authority to classify and control access to information bearing on national security" is based upon the President's constitutional power as the "Commander in Chief of the Army and Navy of the United States." *Egan*, 484 U.S. at 527. Because this power is rooted in the Constitution, separation of powers is implicated and bars judicial review of any exercise of that power, at least where, as here, no specific statute purports to provide to the contrary. Therefore, consistent with *Egan*, the judiciary may not review the present access determination made under Executive Order 12356.

Indeed, at least two courts have held that the reasoning in *Egan* and *Webster*[4] supports the conclusion that, under separation of powers, security clearance determinations are not judicially reviewable, at least not without a clear, strong declaration from Congress. *See Dorfmont v. Brown*, 913 F.2d 1399, 1401 (9th Cir. 1990), *cert. denied*, 111 S. Ct. 1104 (1991) (*Egan*'s analysis "applies no less to the federal courts than to the MSPB. When it comes to security matters, a federal court is 'an outside nonexpert body.'"); *Guillot v. Garrett*, 970 F.2d 1320, 1325 (4th Cir. 1992) (stating that an "unmistakable expression of purpose . . . would be required to support a conclusion that Congress intended to subject the Executive's security clearance determinations to scrutiny"). *See also Chicago & Southern Air Lines, Inc. v. Waterman Steamship Corp.*, 333 U.S. 95, 111 ("[T]he very nature of executive decisions as to foreign policy is political, not judicial. . . . They are decisions of a kind for which the Judiciary has neither aptitude, facilities nor responsibility and which has long been held to belong in the domain of political power not subject to judicial intrusion or inquiry.").

[4] In *Webster*, the Supreme Court concluded that there was no authority under the Administrative Procedure Act to review a termination of a Central Intelligence Agency employee on the ground of a potential "threat to security." *Webster*, 486 U.S. at 595, 601. The Supreme Court concluded that the agency's termination decision was "committed to agency discretion by law" and was thus not reviewable. *Webster*, 486 U.S. at 600-01 ("[W]e see no basis on which a reviewing court could properly assess an Agency termination decision.").

The same reasoning applies to the Court of Federal Claims. Whether that court is considered an Article I or an Article III court, the access decisions of the Executive may not be countermanded by *either* coordinate Branch. Thus, we conclude that the Secretary of the Air Force's determination under Executive Order 12356 concerning the number of persons who shall have access to the programs is not reviewable by the Court of Federal Claims.

C. Future Litigation of This Case

The court's control over the scope of discovery, however, remains undiminished. The panoply of enforcement tools given to the trial court under the rules and the case law also remains available.

The parties are hereby specifically notified that they should not contemplate resolving routine discovery disputes -- those not involving lack of judicial authority -- by resort to mandamus. Normally, of course, discovery rulings are not subject to review by mandamus.

We note with dismay that most of both parties' submissions were devoted not to dispassionate exposition of the dispositive legal issue, but rather to heated reciprocal charges of bad faith, past foot-dragging in discovery, predictions about vast increases in future discovery requests or unreasonable opposition thereto and other clearly extraneous or speculative matters. A more disciplined and professional approach by all counsel will be required if this case is to proceed properly.

Finally, the trial court will have to find ways to manage the pace of discovery that do not usurp the power to grant access to classified, compartmented data. Under the Executive Order, the only legal authority applicable here, such access decisions are exclusively for the Executive or his delegatee. Perhaps the circumstances under which the 10 authorized individuals review the documents in the two Special Access Programs can be made more efficient. We have confidence the trial court can find means that do not breach the Separation of Powers or contravene *Egan*.

CONCLUSION

Mandamus is traditionally used, *inter alia*, to confine a trial court "to a lawful exercise of its prescribed jurisdiction . . . ." *Gulfstream Aerospace Corp. v. Mayacamas Corp.*, 485 U.S. 271, 289 (1988). But the party seeking mandamus must show that the right to the issuance of a writ is "clear and indisputable." *Id.* We conclude that the United States has shown that the Court of Federal Claims did exceed the "lawful exercise of its prescribed jurisdiction" and that the United States has shown its right to the requested relief to be "clear and indisputable."

Accordingly,

IT IS ORDERED THAT:

The United States' petition for writ of mandamus is granted. The Court of Federal Claims is directed to vacate its March 5, 1993 order.

FOR THE COURT

19 April 1993
Date

/s/ Paul R. Michel
Paul R. Michel
Circuit Judge

cc: Mary Mitchelson, Esq.
Francis M. Gaffney, Esq.
Herbert L. Fenster, Esq.
United States Court of Federal Claims, Clerk
United States Court of Federal Claims, Judge

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

* * * * * * *

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,

Plaintiffs,

v.

UNITED STATES OF AMERICA,

Defendant.

No. 91-1204C

Filed : April 30, 1993

* * * * * * *

ORDER

Defendant's counsel persist in misinterpreting our concern that defendant not be permitted to exploit secret information for litigation advantage. Defendant knows that sensitive information was used not only to argue Secretary Donley's invocation of the state secrets privilege but also for defendant's earlier litigation needs.

Defendant's attorneys, if not plaintiffs', know why the court has not been able to specify its concerns in each instance. In the future, counsel should not rely on this problem of communication to

misrepresent the record. Such tactics raise serious implications under Rule 11.

We expect that further secret information may appear in this case. Counsel may not use such secret information for its own purposes, and argue that the state secrets privilege precludes disclosing such information to plaintiffs' counsel. Such use jeopardizes the information, gives defendants litigation team an unfair advantage, and undermines proper invocation of the privilege.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

MISCELLANEOUS NO. 374

IN RE UNITED STATES,

Petitioner.

ON PETITION FOR WRIT OF MANDAMUS

Before ARCHER, Circuit Judge, FRIEDMAN, Senior Circuit Judge, and MICHEL, Circuit Judge.

MICHEL, Circuit Judge.

ORDER

The United States petitions for a writ of mandamus to direct the Court of Federal Claims to vacate its April 12 and April 14, 1993 orders requiring the Air Force to grant special access to plaintiffs' counsel to certain classified, special access programs and information controlled by the Air Force for which the Acting Secretary of the Air Force had formally asserted the Military and State Secrets Privilege.[1] The trial court rejected the assertion of

[1] The United States also moved before us for stays of the orders directing disclosure. On April 16, 1993, this court, *ex parte*, temporarily stayed the orders "pending consideration" of submissions. The contractors oppose the stay pending disposition. The United States moves for leave to file a reply, with reply attached. In view of our disposition of the mandamus petition, the United States' motion for a stay

privilege without finding it was improperly or inappropriately invoked and ordered disclosure of the military secrets involved. It denied the government's motion for protective order and for a stay and for certification. The government then filed the instant petition. McDonnell Douglas Corporation and General Dynamics Corporation oppose. Extensive submissions have been filed by both parties. We grant the petition.

BACKGROUND

This is the second government mandamus petition to arise from discovery disputes in a lawsuit by McDonnell Douglas and General Dynamics against the United States because of the Department of the Navy's termination for default of their contract to produce a stealth attack aircraft called A-12 for basing on aircraft carriers. In the suit, McDonnell Douglas and General Dynamics claimed, *inter alia*, that the United Sates breached an implied duty to share with the contractors "superior knowledge" about problems in producing stealth aircraft, and their solution, which was discovered in earlier production of the B-2 and F-117A stealth aircraft by other manufacturers. In this regard, McDonnell Douglas and General Dynamics sought discovery from the Department of the Air Force concerning several classified, special access programs.

A dispute concerning the Court of Federal Claims' authority to review and reverse a

pending disposition and the motion for leave to file a reply are moot.

determination by the Acting Secretary of the Air Force regarding the number of persons granted access to documents subject to "special access" restrictions was the subject of the earlier mandamus petition, misc. no. 370. We issued a writ of mandamus directing the Court of Federal Claims to vacate its order which had required the Air Force to allow two additional persons access to the two special access programs involved there.

The dispute here arises from counsel for McDonnell Douglas and General Dynamics' request for access to certain highly classified information, mostly from *other* special access programs. In contrast to the earlier petition, here the question is not whether the trial court can review the Acting Secretary's decision as to how many individuals may have access to the original data which the government agreed to disclose but whether the trial court may order access for the plaintiffs' counsel for additional special access programs, in the face of the assertion of the Military and State Secrets Privilege.

The following is a chronology of actions by the Court of Federal Claims that created this issue.

A. The Court of Federal Claims' March 18, 1993 Order

The February 1993, plaintiffs' attorneys orally and informally sought intervention by the trial court regarding certain highly classified and compartmented information known to some General Dynamics' employees, to which plaintiffs' attorneys desired access. The government objected. On March 18, 1993, the trial court issued an order stating:

"Defendant may not preclude disclosure of *relevant* Air Force information to plaintiffs' counsel unless it can show that such information may be withheld in accordance with an established privilege." (Emphasis added.)

B. The Court of Federal Claims' March 23, 1993 Order

On March 23, the trial court conducted a hearing to address the issue of disclosure of the requested information to plaintiffs' counsel. Later that same day, the court issued an order stating: "Defendant will disclose to plaintiffs' attorneys information currently being withheld, no later than 5:00 p.m. on Tuesday, March 30, 1993."

On March 30, 1993, the United States moved for a protective order, formally invoking the Military and State Secrets Privilege. The privilege was invoked in an unclassified, public declaration signed by the Acting Secretary of the Air Force, Michael B. Donley. In the declaration, Acting Secretary Donley stated that he "personally review[ed] and consider[ed]" the matters at issue and that he "personally determined" that disclosure of the information "could be expected to cause exceptionally grave damage to national security." The Acting Secretary generally explained the threat to national security and state that an *ex parte, in camera*, classified declaration by him explained the threat more specifically. Both the public declaration and

the *in camera*, classified declaration have been reviewed by the trial court and by this court.[2]

C. The Court of Federal Claims' March 31, 1993 Order

On March 31, the trial court issued an order raising three issues for the government's response. The trial court asserted that the wording of the public declaration raise[s] the question of whether [Acting Secretary Donley] is the proper individual to invoke the privilege." Second, the trial court noted that the declaration does not address the problem of the government's disclosure of "such matters to [government] attorneys in this case *for purposes of this litigation*." (Emphasis added.) Finally, the trial court stated that the United States' motion "does not address the problem of plaintiffs' communications with their attorneys." The trial court also said that "*plaintiffs* have crucial knowledge that is being withheld from *plaintiffs'* counsel." (Emphasis added.)[3] The trial court scheduled a hearing for

[2] On April 19, 1993, Circuit Judge Paul R. Michel met with Colonel Hennessey and Mr. Eames of the Air Force to review Acting Secretary Donley's classified declaration. A summary of this review meeting was appended to an order issued by this court on April 19, 1993, which disposed of a motion to make certain records of the review meeting.

[3] Although the Court of Federal Claims stated in this order that "plaintiffs" have access to the information, they do not. The plaintiffs in this case are two corporate entities, McDonnell Douglas and General Dynamics. These corporate entities themselves do not have possession of the military secrets, for they have not been granted special access by the Air Force Secretary. *Some* of their *employees*, however, have been granted special access by the Air Force Secretary and do know

April 2, 1993 to address these issues further. At the hearing, the United States agreed to produce supplemental declarations to address the trial court's stated concerns, and McDonnell Douglas and General Dynamics informed the trial court that they opposed the government's assertion of privilege.

D. The Court of Federal Claims' April 7, 1993 Order

Following the hearing the United Sates filed a supplemental public declaration and a supplemental classified declaration. On April 7, the Court of Federal Claims issued an order stating:

> [Acting] Secretary Donley has shown the court that he *is the appropriate official* to invoke the states secret doctrine. We have every confidence in [Acting] Secretary Donley and his representative. However, the *rightful* concerns of the Air Force must be *balanced* with the court's concern for the integrity of the adversary process. Plaintiffs must be permitted to discuss *their case* with their counsel.

(Emphasis added.) As noted, however, the employees are not "plaintiffs," it is not "their case" but the corporations' cases and the lawyers are not "their counsel."

the secrets, but have no authority to pass them to *anyone*, except as authorized by the Air Force Secretary. *See* Executive Order 12356.

The court warned that unless the parties could agree to stipulations that would obviate the need for further inquiry into these sensitive access issues, "it will be the Order of this court that the Air Force give to one representative from the McDonnell Douglas litigation team and one from the General Dynamics litigation team a modified briefing."

E. The Court of Federal Claims' April 12, 1993 Order

Because the parties were unable to reach such an agreement, the court issued an order on April 12 stating:

> Defendant invoked the state secrets doctrine to preclude plaintiffs from communicating crucial information to their counsel. Defendant cites no authority for applying the doctrine under these circumstances. We have no choice but to direct the Air Force to provide a modified briefing to an attorney for each plaintiff. and IT IS SO ORDERED. . . . The motion for protective order is DENIED.

By denying the motion for protective order, the court effectively denied the government's assertion of the Military and State Secrets Privilege.

In an effort to protect the classified information from disclosure, the government then moved for a stay of the trial court's order requiring disclosure, and for certification of the court's orders for interlocutory appeal.

F. The Court of Federal Claims' April 14, 1993 Orders

On April 14, the trial court denied the United States' motion for a stay and for certification. In its denial for the motion for certification, the trial court further stated:

> Our denial of defendant's motion [for protective order] was not a rejection of [Acting] Secretary Donley's concern for the *sensitivity of the matters described* in his *in camera* affidavit. *We did not reach the merits of the [Acting] Secretary's determination.* The issue is not whether plaintiffs may be afforded access to classified information. The issue is whether *plaintiffs* must be permitted to discuss such information with their attorneys for purposes of this litigation.

(Emphasis added.)

In the order, the court noted that the plaintiffs' attorneys had top secret security clearances and that the government's counsel did not deny having been granted access to the same information over which the privilege was asserted. The court concluded that because the plaintiffs' attorneys were denied access to the information, the "prejudice to plaintiffs . . . is manifest." Accordingly, the court *ordered*: "Defendant will permit plaintiffs to disclose the information ordered on April 12 to their attorneys no later than 2:00 p.m. on April 16, 1993."

On April 16, the United States filed this petition for writ of mandamus for vacatur of the trial court's disclosure orders. This court, *ex parte*, temporarily stayed the orders pending "consideration" of submissions. As in the earlier mandamus case, the dispositive issue is whether the trial court has legal authority to reverse special access decisions made by a service secretary under Executive Order 12356. That it does not is even clearer in this case where the Military and State Secrets Privilege has been formally invoked as to data that requires special access and the court does not question the legitimacy of the classification or the "sensitivity" of the information. Therefore, we grant the writ.

DISCUSSION

In *United States v. Reynolds*, 345 U.S. 1 (1953), the Supreme Court explained the considerations for discerning a proper invocation of the Military and State Secrets Privilege. The Court said:

> The privilege belongs to the Government and must be asserted by it; it can neither be claimed nor waived by a private party. It is not to be lightly invoked. There must be a formal claim of privilege, lodged by the head of the department which has control over the matter, after actual personal consideration by that officer. The court itself must determine whether the *circumstances are appropriate for the*

> *claim* of privilege, and yet do so without forcing a disclosure of the very thing the privilege is designed to protect.

Id. at 7-8 (footnotes omitted) (emphasis added). We address these factors seriatim.

A. Head of the Department

1. *Personal consideration by appropriate official.* In its April 7, 1993 order, the Court of Federal Claims stated that "[Acting] Secretary Donley has shown the court that he is the appropriate official to invoke the states secret doctrine." Neither party disputes that finding. Nor is it disputed that Acting Secretary Donley personally assessed the basis for the assertion of the privilege and formally asserted the claim of privilege.

2. *Special access determinations are committed by law solely to the agency head.* As set forth in more depth in our April 19, 1993 order in *In re United States*, misc. no. 370, the grant of a security clearance or the authority to determine who or how many persons shall have access to classified information "is committed by law to the appropriate agency of the Executive Branch." *Department of Navy v. Egan*, 484 U.S. 518, 526-27 (1988). In this case, the member of the Executive Branch who possesses the authority to grant access is the agency head, Acting Secretary of the Air Force Donley. The Acting Secretary derives his authority from Executive Order 12356 which prescribes a uniform system for classifying, declassifying, and safeguarding national security information. The Acting Secretary's authority under the Executive

Order derives, in turn, from the constitutional grant of power to the Executive to command the military and to conduct foreign affairs. The kinds of decisions made by agency heads under the Executive Order necessarily are "predictive judgments" delegated solely to them because they "bear the responsibility for the protection of classified information" and not to "outside non-expert bod[ies]," such as administrative agency boards, *Egan*, 484 U.S. at 529, or courts. In short, it is clear that the Acting Secretary was the *only* person who had the authority to decide whether this information could be disclosed to counsel, and therefore, his assertion of the privilege is dispositive unless the assertion is shown to be inappropriate, unlawful or fraudulent. No such contention is made here.

By ordering a "modified briefing," the trial court clearly usurped the exclusive authority of the Acting Secretary. As the contractors' brief repeatedly indicates, the trial court independently assessed what was adequate to protect national security. The contractors state that the trial court "permit[ted] partial disclosure based on careful scrutiny of the *in camera* submissions," and that "the trial court properly scrutinized the material with care and concluded that the Government's invocation of the privilege did not preclude a 'modified briefing.'" As characterized by the contractors, "*the court* concluded that the 'modified briefing' would not pose a danger to national security." (Emphasis added.) Such risk assessment, however, is precisely the type of "predictive judgment" that the Supreme Court in *Egan* stated was one exclusively for the

Executive.[4] Such risk assessments are beyond the competence of courts and their authority.

B. "Appropriate Circumstances" for the Assertion of the Privilege

As a matter of law, "[t]he occasion for the privilege is appropriate" if the court is satisfied, "from all circumstances of the case, that there is a reasonable danger that compulsion of the evidence will expose military matters which, in the interest of national security, *should not be divulged*." *Reynolds*, 345 U.S. at 10 (emphasis added). Although the Court of Federal Claims stated in it April 14, 1993 order that it "did not reach the merits of the [Acting] Secretary's determination," the court effectively denied the merits of the Acting Secretary's assertion of the Military and State Secrets Privilege by denying the government's motion for protective order. By ordering a "modified briefing," the court rejected the Acting Secretary's assertion of the Military and State Secrets Privilege and usurped his exclusive power to grant access to special access programs and other classified matter under Executive Order 12356. What, exactly, the trial court meant to include or exclude in the "modified

[4] The contractors assert that "the instant mandamus petition does not deal with any issue involved in [*Egan*], and the government has not cited *Egan* as support for its argument." While the government does not cite *Egan*, the government's argument implicitly implicates it. The government states: "[I]n devising and attempting to implement a 'modified briefing' procedure, wholly of its own creation, the trial court is attempting to undertake the actual micro-management of control over this Nation's military secrets."

briefing" is unclear. But what is clear is that it would *necessarily include* information in some form from other special access programs beyond those for which counsel have previously been granted access by the Air Force Secretary. The contractors do not deny this. Rather, they simply state that "the court below did not order that *all* classified information in the Government's possession concerning the matters at issue be disclosed to Plaintiffs' counsel." (Emphasis added.) By this statement, the contractors effectively admit that the court did order disclosure of some of the classified, compartmented information.

Rather than considering whether there was a "reasonable danger" that military secrets would or could be divulged if production of the information was compelled, as required by *Reynolds*, the Court of Federal Claims instead considered and explicitly based its disclosure orders on the following: (1) the two attorneys who sought the information had already been granted top security clearances and access to *other* compartmented programs; (2) Some of General Dynamics' employees have the information and "must" have a right to disclose the information to counsel; and (3) the Air Force has disclosed the information to the United States' counsel "for purposes of this litigation." We conclude that these three considerations are wholly irrelevant under controlling case law and legally could not substitute for the sole inquiry required under *Reynolds*: whether there is a "reasonable danger" that military secrets would or could be divulged if production of the data is compelled. Further, we hold that here

the circumstances were "appropriate" for assertion of the Military and State Secrets Privilege. Indeed, the trial court did not question the basis for asserting the privilege, stating that it did not reach that issue.

(1) While the Court of Federal Claims correctly noted that the contractors' attorneys have been granted access to *certain* compartmented programs, this cannot mean that they thereby are also granted access to *other* special access programs. The system of special access programs specifically contemplates that no matter how trustworthy an individual, he may not have access to a particular program except if specifically granted it by the service secretary pursuant to the criteria of Executive Order 12356. As explained by Acting Secretary Donley in his public declaration:

> An individual [employed by a Defense contractor] may have access to one special access program while his colleagues have access to different special access programs. Despite the fact that the individuals are professional colleagues, that they possess the requisite security clearances, and they work in the same secure facility, such individuals are still prohibited, absent being given access to another program, to share special access information across program boundaries.

See Executive Order 12356, § 4.2. Indeed, the contractors admit in their "Opposition to Petition for

Writ of Mandamus" that "[t]his case is materially unlike any other in which issues of state secrets privilege have arisen" because "the specific subject matter of the contract at issue included the development and use of classified, *compartmented* stealth technologies." (Emphasis added.) What they do not acknowledge, however, is that this fact makes it all the clearer that the trial court lacked authority to order disclosure.

(2) Similarly, even though certain employees of General Dynamics have knowledge of the special access information sought by counsel, assertion of the privilege may properly preclude future disclosure of that information *to anyone*, including the contractors' counsel. *See Farnsworth Cannon, Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (*en banc*) (application of the State Secrets Privilege prevented information from being shared with plaintiff's attorney); *see also Fitzgerald v. Penthouse Int'l, Ltd.*, 776 F.2d 1236, 1242 n.8 (4th Cir. 1985) (privilege requires dismissal of case thereby preventing disclosure at trial of classified information despite the fact that one of the parties had "personal knowledge of classified matters within the scope of the state secrets privilege"). Thus, the fact that these employees already have access to the compartmented information sought here does not divest the service secretary of his exclusive authority to control access to other persons or limit his right to assert the privilege to prevent *any* disclosure in a pending lawsuit. *See Northrop Corp. v. McDonnell Douglas Corp.*, 751 F.2d 395, 402-03, n.9 (D.C. Cir. 1984) ("prior disclosure of similar information does

not preclude the potential for harm" in future disclosure).

The contractors argue that "the trial court was rightly concerned about the effect of the Government's attempted privilege invocation on Plaintiffs' ability to discuss information with counsel, thereby potentially infringing upon Plaintiffs' constitutional right to counsel." Similarly, the contractors assert that the First Amendment also protects the contractors right to confer with their counsel. These arguments are unpersuasive. Because application of the Military and States Secrets Privilege can require complete dismissal of a case, *Ellsberg v. Mitchell*, 709 F.2d 51, 65 (D.C. Cir. 1983), *cert. denied sub nom. Russo v. Mitchell*, 465 U.S. 1038 (1984), any subsidiary limitation on conferring with counsel which might otherwise be precluded by the constitution cannot apply here.

(3) Finally, the fact that the government's attorneys may have reviewed the information at issue here (mistakenly or not) is irrelevant to whether the privilege is still available to prevent disclosures to others. Under the special access rules of Executive Order 12356, each program is separate and each potential "accessee" is a separate issue. Disclosure to anyone beyond those individuals specially granted access by the service secretary whether they be within the government or within the same corporation as those previously granted access is strictly forbidden and indeed would create criminal liability. *Cf. Halkin v. Helms*, 598 F.2d 1, 9 (D.C. Cir. 1978) ("The government is not estopped

from concluding in one case that disclosure is permissible while in another case it is not."). As correctly noted by the United States in its petition, the United States may not use this information in the litigation, even though the trial court, apparently incorrectly, said the government attorneys had the information for purposes of this litigation.[5] That the United States' attorneys may have reviewed the compartmented information at issue here is entirely irrelevant to whether there would be a "reasonable danger" to national security if the information is released to someone new, including the contractors' attorneys in connection with this lawsuit. Under *Reynolds*, that is the sole issue that is judicially reviewable.

The trial court erred in this case because it based its decision on extraneous concerns and ignored the sole legal test required by the Supreme Court in *Reynolds*. The trial court should have confined itself solely to whether there was a "reasonable danger that compulsion of the evidence will expose military matters which, in the interest of

[5] It does not appear that the government has the information "for purposes of the litigation." Although certain government attorneys may be *aware* of the information, that does not mean that the government has the information for the litigation. Contrary to the trial court's statement that "the defendant's attorneys have used such information for tactical purposes involving the merits of plaintiffs' superior knowledge claim," nothing in the submissions indicates that the government has so used the information. To have used the information, it seems the government would have had to file *ex parte* submissions for consideration by the judge. No such submissions appear to have been made.

national security, should not be divulged". *Reynolds*, 345 U.S. at 10. Courts must give "utmost deference" to necessarily speculative projections contained within such assertions of privilege. *See Halkin*, 598 F.2d at 9 ("Courts should accord the 'utmost deference' to executive assertions of privilege upon grounds of military or diplomatic secrets.") (quoting *United States v. Nixon*, 418 U.S. 683, 710 (1974)).

In its March 31, 1993 order, the Court of Federal Claims sought to use language from *Reynolds* to support its position: "Judicial control over the evidence in a case cannot be abdicated to the *caprice* of executive officers." *See Reynolds*, 345 U.S. at 9-10 (emphasis added). But this dicta was not written in a vacuum and can mean no more than that the Executive must have a rational basis for its security concern. Plaintiffs do not assert that it did not. Nor did the trial court. Thus, here there is no "caprice." Similarly, the contractors' argument that "[d]eference to the executive's allegations of harm does not mean unquestioning acceptance of every claim of privilege" is unpersuasive. As explained below, neither this court nor the Court of Federal Claims accepted the government's assertion of the privilege "unquestioned." Rather both courts have thoroughly reviewed the Acting Secretary's declarations. Neither court saw any need for *in camera* review of the underlying documents, the only further step permitted by *Reynolds*.

Moreover, the Supreme Court in *Reynolds* specifically prohibited trial courts from basing rulings on privilege on their assessment of the

parties' *need* for the information. The Supreme Court concluded that "even the most compelling necessity [for discovery of the information] cannot overcome the claim or privilege if the court is ultimately satisfied that military secrets are at stake," *id.*, at 11, *i.e.*, that the classification was not fraudulent or incorrect and the documents did in fact contain military secrets. Plaintiffs do not contend otherwise. Thus, the repeated references in the trial court's orders that the information is "crucial" and "relevant" are not proper considerations in the face of the assertion of the privilege.[6]

[6] We need not decide the degree of importance of the information at issue to the contractors' ability to prove their case as alleged. The United States admits that some courts have placed emphasis on the degree of necessity that a party has for the information, citing *American Civil Liberties Union v. Brown*, 619 F.2d 1170, 1173 (7th Cir. 1980) (*en banc*) (vacating the district court's order requiring production of documents despite assertion of the State Secrets Privilege and remanding for an *in camera* determination of the necessity for the records sought *because* the claim of state or military secrets appeared "dubious") and *Jabara v. Kelley*, 75 F.R.D. 475 (E.D. Mich. 1977). We view Brown and Jabara as support for no more than that the trial court may require ex parte *in camera* inspections of information if necessity for the information is great, and *if* assertion of the State Secrets Privilege seems questionable. This reading of *Brown* and *Jabara* is consistent with *Reynolds*. *See Reynolds*, 345 U.S. at 11. In the present case, neither the trial court nor the plaintiffs even argued that the Acting Secretary's invocation of the privilege was dubious. On the contrary, the trial court characterized the Acting Secretary's national security concerns as "rightful." In any event, we hold, *post*, that the assertion was "appropriate."

Similarly, the trial court's references to "balancing" the interests of the government against those of the plaintiffs is also an impermissible legal test under *Reynolds*. The contractors' argument that "*Reynolds* requires that such a balancing be performed by the court to determine the validity of the privilege claim" is incorrect. In support of its argument, the contractors quote the following language from *Reynolds*: "In each case, the showing of necessity which is made will determine how far the court should probe in satisfying itself that the occasion for invoking the privilege is appropriate. Where there is a strong showing of necessity, the claim of privilege should not be lightly accepted . . . ." *Id.* The balancing that is suggested by this quotation, however, is not directed to the court's ultimate acceptance or denial of the privilege. Rather, it refers to the trial court's decision as to whether or not something more than just the Acting Secretary's declaration should be reviewed. In other words, in determining whether or not to review the underlying documents, the court may balance the contractors' need for the information against the dubiousness of the government's assertion of the privilege. Once the determination is made whether to require a closer examination of the assertion of the privilege, however, the contractors' need for the information plays no part in a trial court's determination of whether there is a reasonable danger that national security would be threatened by release of the information. *Reynolds*, 345 U.S. at 11 ("even the most compelling necessity cannot overcome the privilege if the court is ultimately

satisfied that military secrets are at stake"); *Ellsberg*, 709 F.2d at 57 ("When properly invoked, the state secrets privilege is absolute. No competing public or private interest can be advanced to compel disclosure of information found to be protected by a claim of privilege."); *Halkin v. Helms*, 690 F.2d 977, 990 (D.C. Cir. 1982) ("[T]he critical feature of the inquiry in evaluating the claim of privilege is not a balancing of ultimate interests at stake in the litigation. That balance has already been struck.").

It is apparent that the Court of Federal Claims did recognize that military secrets were at stake. *See, e.g.*, Order of April 7, 1993 (trial court characterizes the Acting Secretary's national security concerns as "rightful"). But whatever the trial court's view, based on our own review of the classified declaration of Acting Secretary Donley, we agree that the United States has established that there is a "reasonable danger that compulsion of the evidence will expose military matters which, in the interest of national security, should not be divulged." *Reynolds*, 345 U.S. at 10.[7] Therefore, the Court of Federal Claims exceeded its authority in compelling the Air Force to disclose the information to anyone else, even plaintiffs' attorneys.

The contractors argue, finally, that mandamus should not issue because the court's orders that the

[7] As explained *supra* note 2, this court has inspected the classified declaration of Acting Secretary Donley. That declaration specifically and convincingly explains the highly sensitive nature of the military secrets at stake and the legitimacy of their classification at the very highest levels.

plaintiff's counsel be given a "modified briefing" is consistent with the requirement of *Ellsberg*, 709 F.2d at 57, that the government's assertion of the privilege should be scrutinized on an item-by-item basis. In *Ellsberg*, the court did not allow State Secrets Privilege protection for one aspect of the plaintiffs' discovery requests. In particular, the plaintiffs requested to know *which* Attorneys General authorized a particular surveillance. Because "the government [did] not even purport to explain" why the information must be withheld, the court required disclosure. *Id.* at 60. Thus, although it is true that the court has the power to disentangle sensitive information from non-sensitive information, in this case the contractors have not even alleged the government's assertion of the privilege is too broad or that it covers any nonsensitive of the privilege is too broad or that it covers any nonsensitive information. Rather, in this case all of the information over which the government has asserted the privilege is plainly sensitive. *Compare In re United States*, 872 F.2d 472, 478 (D.C. Cir. 1989) (stating that an item-by-item determination of the applicability of the State Secrets Privilege was appropriate because, *inter alia*, a portion of the requested information had already been obtained by plaintiff under Freedom of Information Act, 5 U.S.C. § 552 (1982)).

Moreover, the trial court apparently did not scrutinize the information over which the privilege was asserted in an effort to segregate any nonsensitive information. There is nothing in the submissions to show that the trial court ever

requested or reviewed the underlying documents or stated that it determined any specific document to be non-sensitive. Rather the trial court's order requiring a "modified briefing" applied generally to the requested information.[8]

CONCLUSION

Mandamus is traditionally used, *inter alia*, to confine a trial court "to a lawful exercise of its prescribed jurisdiction . . . ." *Gulfstream Aerospace Corp. v. Mayacamas Corp.*, 485 U.S. 271, 289 (1988). A party seeking mandamus, however, must show that the right to the issuance of the writ is "clear and indisputable." *Id.* We hold that on the record in this case, the United States has shown that the Court of Federal Claims exceeded the "lawful exercise of its prescribed jurisdiction" and the United States has shown that its right to the requested relief is "clear and indisputable." Therefore, we grant the writ.

Accordingly,

IT IS ORDERED THAT:

The United States' petition for writ of mandamus is granted. The Court of Federal Claims is directed to vacate its April 12 and April 14, 1993 disclosure orders.

[8] The fact that the concept of a "modified briefing" apparently resulted from an informal conversation with Colonel Hennessey also suggests that the court did not scrutinize the documents in order to segregate nonsensitive information from sensitive information.

FOR THE COURT

30 April 93
Date

/s/Paul R. Michel
Paul R. Michel
Circuit Judge

cc: Mary Mitchelson, Esq.
Francis M. Gaffney, Esq.
Herbert L. Fenster, Esq.
United States Court of Federal Claims, Clerk
United States Court of Federal Claims, Judge

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

* * * * * * *

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,

Plaintiffs,

v.

UNITED STATES OF AMERICA,

Defendant.

* No. 91-1204C

* Filed: May 7, 1993

* * * * * * *

ORDER

Defendant has refused to grant plaintiffs' request for two additional persons with access to B-2 and F-117A information, and invoked the state secrets doctrine to prevent a plaintiff's employee from communicating relevant information to plaintiffs' attorneys. The Federal Circuit ruled that such restrictions on plaintiffs' discovery cannot be questioned by this court.

Plaintiffs' attorneys have demonstrated on the record they cannot make effective use of information remaining in the B-2 and F-117A programs under

the limitations imposed by defendant. To the extent that such information exists elsewhere, plaintiffs' attorneys will be denied access. Thus, plaintiffs may be precluded from relying on superior knowledge as a defense to default termination. Our experience with this case and with the Government's use of classified materials persuade us that plaintiffs probably cannot prove Count IX of their complaint.

It is not necessary for a court to serve the appearance of discovery when its knowledge of the case suggests that discovery will not be productive. *See Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 548 (2nd Cir. 1991). This is especially true where sensitive military information could be exposed to scrutiny in a futile exercise.

Therefore, it is ORDERED that:

1. All discovery related to Air Force programs is stayed indefinitely. Plaintiffs will not seek further information from the B-2 or F-117A programs without leave of this court.

2. All discovery related to plaintiffs' allegations of superior knowledge is stayed pending a determination by this court whether Count IX or any other claim or defense must be dismissed. *See Zuckerbraun*, 935 F.2d at 547.

3. Plaintiffs or defendant may request a hearing to address this Order or related issues; the court is available to the parties at any time for this purpose.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

No. 91-1204C
(Judge Hodges)

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and
GENERAL DYNAMICS CORPORATION,

Plaintiffs,

v.

THE UNITED STATES,

Defendant.

DEFENDANT'S MOTION TO DISMISS PLAINTIFFS' "SUPERIOR KNOWLEDGE" CLAIMS, OR IN THE ALTERNATIVE, FOR PARTIAL SUMMARY JUDGMENT, AND MOTION FOR A PROTECTIVE ORDER

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IN THE UNITED STATES COURT
OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DEFENDANT'S MOTION TO DISMISS PLAINTIFFS' "SUPERIOR KNOWLEDGE" CLAIMS, OR IN THE ALTERNATIVE, FOR PARTIAL SUMMARY JUDGMENT, AND MOTION FOR A PROTECTIVE ORDER

Plaintiffs' "superior knowledge" claims are inextricably intertwined with information that is protected by the military state secrets privilege. Accordingly, it is not possible to continue to litigate plaintiffs' superior knowledge claims, and those claims must be dismissed.

Specifically, plaintiffs' novel "superior knowledge" claims turn upon information that may or may not exist in top secret, special access, unacknowledged programs that themselves may or may not exist. It is not possible for the Government

to confirm or deny plaintiffs' allegations, to respond to their discovery requests, or to divulge information which would establish, or refute, plaintiffs' "superior knowledge" claims, or the Government's factual defenses to those allegations.

Because plaintiffs' superior knowledge claims must be dismissed, continued discovery regarding classified, special access information would be futile, and, more importantly, would needlessly endanger national security. Accordingly, a permanent protective order, in the nature of the Court's stay order dated May 7, 1993, should be entered.

BACKGROUND AND STATEMENT OF FACTS

This lawsuit arises out of the Navy's termination for default of a contract with the "team" of McDonnell Douglas Corp. and General Dynamics Corp. (collectively "plaintiffs"). The contract was for production of a carrier-based low-observable stealth attack aircraft, referred to as the "A-12." Plaintiffs failed to perform their obligations under the A-12 contract in accordance with agreed-upon specifications and schedules, and the Navy therefore appropriately terminated the contract for default. In this lawsuit, plaintiffs purport to challenge that default termination.

I. Plaintiffs' "Superior Knowledge" Claims

Plaintiffs, understandably, have been anxious to divert attention from their performance failures under the A-12 contract. Accordingly, over the past year, plaintiffs have focused their efforts (and, consequently, the energies of the Government and

the Court) not upon the A-12 contract at issue, but upon various other programs within the Department of Defense.

Toward that end, principally in Count IX of their Second Amended Unclassified Complaint, plaintiffs McDonnell Douglas Corporation and General Dynamics Corporation have alleged that the Government breached an implied contractual duty, by not sharing with plaintiffs classified information that was contained in compartmentalized, and even covert or unacknowledged, programs.

As the Court is well aware, it remains the Government's position that no such duty may be implied, as a matter of law, in part because such a duty would render meaningless the careful "special access" restrictions that the Executive has imposed in order to protect this nation's most vital military secrets. *See generally Department of Navy v. Egan*, 484 U.S. 518 (1988); Executive Order 12,356 sec. 4.2 (April 2, 1982), 3 C.F.R. 166, 174 (1983). Moreover, unlike any contractor who has ever pursued a "superior knowledge" claim, the plaintiffs in this case have steadfastly refused even to identify what the allegedly unshared "superior knowledge" was, except to aver that the information was contained in classified, special access programs. *E.g.*, Second Amended Unclassified Complaint ¶¶ 46, 271, App. 2, 5.

The Government therefore moved to dismiss those portions of the complaint that were based upon an alleged implied contractual duty to share classified information contained in

compartmentalized, special access programs. The Court denied our motion to dismiss, but indicated that discovery upon those superior knowledge claims should be "limited severely." *E.g.* App. 8.[1]

II. Plaintiffs' Discovery Directed Toward The Department Of The Air Force's B-2 And F-117A Programs: The First Mandamus Opinion

Initially, plaintiffs restricted their inquiries to the Department of the Air Force's B-2 and F-117A programs. Despite the Court's admonitions and plaintiffs' representations to the contrary, however, plaintiffs' first B-2 and F-117A discovery requests were extraordinarily overbroad. Over the ensuing months, the parties, with the Court's assistance, were able to narrow somewhat plaintiffs' requests for information in the B-2 and F-117A programs.

Because the B-2 and F-117A information eventually requested by plaintiffs consisted of material that could be shared in this lawsuit without increasing the risk to national security by an unacceptable margin, and because the Secretary of the Air Force desired to assist the Court and to

[1] The Court also denied our subsequent motion to certify the denial of our motion to dismiss, for interlocutory appeal. It remains the Government's position that, as a matter of law, there can be no implied contractual duty to share classified, special access information. We continue to reserve our position on that point for appeal, and would welcome an opportunity to pursue a certified appeal regarding that issue, at any time.

facilitate this litigation, the Secretary determined to provide to plaintiffs and their counsel limited access to the requested materials and information. After plaintiffs negotiated protective orders with the builders of the B-2 and F-117A aircraft, discovery commenced with respect to those programs.[2]

The parties and the Court soon reached a conflict over the appropriate limitations upon access and dissemination of the sensitive military information contained in the B-2 and F-117A programs. Plaintiffs sought expanded access, insisting that they could not "survive" unless more representatives were admitted to the programs, App. 19, and that they could not "manage" to prepare their case under the restrictions imposed by the Secretary of the Air Force. App. 20.[3] On March 5,

[2] The fact that protective orders were required at all highlights, yet again, the absurdity of plaintiffs' present "superior knowledge" claims. The protective orders were necessary because the Government *does not itself control* the release of large amounts of the information that plaintiffs seek. Plaintiffs' claim, then, is that the Government breached an implied contractual duty to share certain information that the Government had *no power* to share.

[3] Plaintiffs subsequently recanted those representations, *after* the court of appeals addressed the matter. App. 27 ("As to the B-2 and F-117 we believe that we could regroup, [and] review the information with ten people. . ."). While plaintiffs' reversals on this point may shed some light upon the general veracity of their representations to the

1993, the Court ordered the expanded access requested by plaintiffs.

On March 9, 1993, the Government filed a petition for a writ of mandamus in the United States Court of Appeals for the Federal Circuit. The appellate court granted our petition on April 19, 1993.

In granting the writ and reversing this Court's March 5, 1993 order, the court of appeals confirmed our position that *Department of Navy v. Egan*, 484 U.S. 518 (1988), "is not distinguishable," with regard to the Executive's exclusive responsibility to control access to classified information. *In re United States*, Misc. No. 370, slip op. at 12 (Fed. Cir., April 19, 1993) (unpublished). The court further emphasized that *Egan*, 484 U.S. 518, and the general deference afforded to Executive decisions regarding classified information, are to be construed "broadly." *Id.*, slip op. at 8 ("[t]he Supreme Court observed, even more broadly, that courts have traditionally been reluctant to intrude upon the authority of the Executive in military and national security affairs"); 13 ("[b]y speaking more broadly . . . , the Court made clear that what was committed exclusively to the

Court, the issue is more fundamental than the number of persons who may review B-2 and F-117A documents. Plaintiffs cannot ever prove their "superior knowledge" claims because those claims are inextricably intertwined with state secrets, not merely because their discovery efforts will, allegedly, be slowed or hindered.

Executive was more than just whether an individual could be denied a security clearance.") (emphasis in original).

The mandate of the opinion was limited to the specific increased access issue before the appellate court. The court of appeals unequivocally affirmed, however, the constitutional separation of powers principles that formed the basis of our original motion to dismiss: "[g]eneral case law concerning the separation of powers doctrine further supports our conclusion." *In re United States*, Misc. No. 370, slip op. at 17.

On April 20, 1993, pursuant to the direction of the court of appeals, this Court vacated its order for expanded access to the B-2 and F-117A programs.

III. Plaintiffs' Current Unlimited Discovery And Open-Ended Superior Knowledge Claims: The Second Mandamus Opinion

At about the same time that plaintiffs were seeking to expand their access to B-2 and F-117A material for purposes of this litigation, they began to pursue expanded inquires into other matters within the Department of Defense.

It is now apparent that plaintiffs' initial representations that their "superior knowledge" claims could remain limited, App. 9, 14, were false. The breadth of the superior knowledge claims purportedly recited in the complaint have no limit, and potentially implicate every weapons program within the Department of Defense that relates in any way to low observable or associated technologies.

See Second Amended Unclassified Complaint ¶¶ 46-47, 55-59, 269-274, App. 1-5. The discovery that plaintiffs are now pursuing in support of those claims is similarly unlimited, and, because of the expansive nature of plaintiffs' claims, it is now clear that the Government's factual defenses would, necessarily, be similarly broad in scope.

A. The Government's March 30, 1993 Invocation Of The State Secrets Privilege

In February 1993, plaintiffs' attorneys raised with the Court an issue regarding certain highly classified matters, to which plaintiffs' attorneys desired access. As a result of plaintiffs attorneys' remarks, the Court initiated its own inquiry, with security personnel of the Department of the Air Force.

The Court held a hearing on March 23, 1993, wherein the Court imposed an obligation upon the Government to disclose to plaintiffs certain highly classified national security information. 3/23/93 Order, App. 28. At that hearing, plaintiffs' attorneys defined the Government's obligation as ensuring that there are no impediments whatsoever to communications "between attorney and client." App. 30. Plaintiffs' attorneys further suggested that they could not pursue plaintiffs' superior knowledge claims, if national security restraints hampered "our efforts just to learn from our own client what the facts are relating to this dispute, . . . our efforts to draft our own discovery, and our performance of the

basic obligation (to develop plaintiffs' superior knowledge claims)." App. 32.

On March 30, 1993, the Government moved for a protective order, upon the basis that the military state secrets privilege prevented disclosure of the information to which the Court' s prior orders appeared to allude. The nature of the particular privileged material was explained in detail in an *in camera* declaration by the Acting Secretary of the Air Force, and the threat to national security was generally explained in a public declaration. 3/30/93 Donley Decl., App. 34. As the Acting Secretary explained, because of the one-week time constraint imposed upon the Government, the specific privilege assertion on March 30, 1993 was limited to the matters directly implicated by the Court's March 23, 1993 order. The Acting Secretary stated, however, that to the extent that this lawsuit would present "a continuing need for release of classified, special access information related to low observable technology, I will continue to view my responsibility to protect national security as requiring invocation of the military and state secrets privilege." 3/30/93 Donley Declaration ¶ 19, App. 40.

B. The Second Mandamus Opinion

On April 12 and 14, 1993, the Court ordered disclosure of information for which the Acting Secretary of the Air Force had asserted the military state secrets privilege, and specifically directed the Air Force to provide a "modified briefing" to plaintiffs' lawyers. Again, we sought a petition for a writ of mandamus from the court of appeals.

On April 30, 1993, the appellate court granted the second petition, and reversed this Court's disclosure orders. The court of appeals rejected plaintiffs' position that the Government may be compelled to grant access to highly classified information "from *other* special access programs." *In re United States*, Misc. No. 374, slip op. at 3 (Fed. Cir., April 10, 1993) (unpublished) (emphasis in original). The court held that the Government' s right to withhold sensitive military information is "all the clearer" when that information is contained in "special access" programs.[4] *Id.*, slip op. at 14. The court of appeals also noted that because some circumstances can require "complete dismissal" of a claim, subsidiary limitations upon the litigation process are not precluded. *In re United States*, slip op. at 15.

ARGUMENT
SUMMARY OF ARGUMENT

Plaintiffs' "superior knowledge" claims violate fundamental constitutional separation-of-powers principles, *e.g.*, *Department of Navy v. Egan*, 484 U.S. 518 (1988), and should therefore be dismissed as a matter of law.

Alternatively, because the very subject matter of plaintiffs' "superior knowledge" claims involve state secrets, those claims cannot be litigated, and

[4] That is *precisely* the sort of information that lies at the heart of plaintiffs' superior knowledge allegations. *See* Second Amended Unclassified Complaint ¶¶ 46; 269-274, App. 1-5.

must be dismissed. In this regard, plaintiffs' "superior knowledge" case is exactly like *Molerio v. F.B.I.*, 749 F.2d 815 (D.C. Cir. 1984), *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544 (2d Cir. 1991), *Bareford v. General Dynamics Corp.*, 973 F.2d 1138 (5th Cir. 1992), *cert. denied*, 113 S. Ct. 1843 (1993), and the host of other authorities that have held dismissal to be required where " 'the merits . . . are inextricably intertwined with privileged matters.'" *Guong v. United States*, 860 F.2d 1063, 1066 (Fed. Cir. 1988), (*quoting Fitzgerald v. Penthouse International, Ltd.*, 776 F.2d at 1243 n.11), *cert. denied*, 490 U.S. 1023 (1989).

Finally, continued "superior knowledge" discovery would unnecessarily endanger national security, and, as in *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544 (2d Cir. 1991), such continued discovery should be disallowed.

I. The Judicially-Created Doctrine Of "Superior Knowledge" Cannot Be Applied To Require The Government To Share Classified, Special Access Information

Application of the "superior knowledge" doctrine in the context urged by plaintiffs would violate the Executive's exclusive constitutional responsibility to exercise its judgment and expertise, in determining with whom "special access" military secrets will be shared. *E.g.*, *Department of Navy v. Egan*, 484 U.S. 518 (1988); Executive Order 12,356 sec. 4.2 (April 2, 1982), 3 C.F.R. 166, 174 (1983). Therefore, plaintiffs' claims are deficient as a matter of law, and should be dismissed.

The United States Court of Appeals for the Federal Circuit, in the two mandamus opinions recently issued in this case, broadly, explicitly and unequivocally rejected the notion that this Court may directly impose a duty upon the Government to disclose classified, special access information to plaintiffs. *See In re United States*, Misc. No. 370, slip op. at 8 ("*Egan* is not distinguishable"); *In re United States*, Misc. No. 374, slip op. at 14 (lack of duty to disclose "all the clearer" when the information is contained in special access programs) .

Plaintiffs' "superior knowledge" claims, however, are based upon allegations of a judicially-created contractual duty to disclose that *same* sort of "special access" information. *See* Second Amended Unclassified complaint ¶¶ 46-47, 55-59, 269-274, App. 1-5. It necessarily follows, from the rulings by the court of appeals, that no such implied duty of disclosure may be imposed upon the Government in this case. Just as this Court may not "reverse special access decisions made by a service secretary under Executive Order 12356," *In re United States*, Misc. No. 374, slip op. at 8, plaintiffs may not dictate reversal of "special access decisions made by a service secretary," under the guise of alleging an implied contractual duty to share superior knowledge.

Because plaintiffs' claims are deficient as a matter of law, they should be dismissed.

II. Invocation Of The Absolute State Secrets Privilege In These Circumstances Was Necessary, Appropriate And Justified

The propriety of the Government's invocation of the state secrets privilege in this case has, of course, been conclusively established by the court of appeals. *E.g.*, *In re United States*, Misc. No 374, slip op. at 13 ("we hold that here the circumstances were 'appropriate' for assertion of the Military and State Secrets Privilege."). As the court of appeals instructed in this case, material that is contained in "special access" programs created and administered pursuant to Executive Order 12,356 is the paradigm of information that is properly subject to the state secrets privilege. *Id.*, slip op. at 21 ("in this case all of the [special access] information over which the government has asserted the privilege is plainly sensitive.")

There can be no question regarding the appropriateness of the Government's invocation of the state secrets privilege in this case.

III. Because The Very Subject Matter Of Plaintiffs' Superior Knowledge Claims Involve State Secrets, Those Claims Must Be Dismissed

Plaintiffs' superior knowledge claims must be dismissed because: (a) the very subject matter of those claims, and the Government's defenses, involve state secrets; (b) the authorities overwhelmingly indicate that dismissal in such circumstances is required; and (c) a host of compelling policies and interests support dismissal of the claims, including the inability of the judicial process to reach a true or

just result in these circumstances, and heightened threats to national security that would result from continued litigation of the claims.

A. The Very Subject Matter Of Plaintiffs' Superior Knowledge Claims Involve State Secrets

Plaintiffs assert that the Government breached its implied contractual duty to share superior knowledge, by not disclosing information contained in other compartmentalized, special access, and unacknowledged programs. *E.g.*, Second Amended Unclassified complaint " ¶¶ 46-47, 55-59, 269-274, App. 1-5. Putting aside for the moment the above-described legal insufficiency of such claims, plaintiffs' allegations, and the Government's factual defenses to such claims, would be inextricably intertwined with information that cannot be disclosed because of the military state secrets privilege.

i. The Legal Elements Of Plaintiffs' Superior Knowledge Claims Necessarily Implicate State Secrets, In These Circumstances

In order for plaintiffs to prevail upon their claims, it would be necessary to determine, *inter alia*: (1) whether plaintiffs actually had vital knowledge of whatever facts they settle upon as constituting "superior knowledge," from other sources; (2) whether the Government was aware that the contractors had no knowledge of, or reason to obtain, the information; and (3) whether the Government, in fact, supplied the relevant information in another

context, and the contractors, for competitive or other reasons, merely failed to take steps to utilize the information at their disposal. *E.g., GAF Corp. v. United States*, 932 F.2d 947, 949 (Fed. Cir. 1991), *cert. denied*, 112 S. Ct. 965 (1992).

Any claim for a breach of the implied duty to share superior knowledge, then, turns upon "specific evidence" relating to the respective information available to the parties, and to any potential sources of that information. *Id.*, 932 F.2d at 949. *See also, American Ship Building Co. v. United States*, 228 Ct. Cl. 220, 225 (1981), *citing, Helene Curtis Industries. Inc. v. United States*, 160 Ct. Cl. 437 (1963); *Glasgow Associates v. United States*, 495 F.2d 765, 769 (Ct. Cl. 1974) ("we find the assertion of superior knowledge here to be factually without merit since plaintiff had sufficient notice [of the alleged superior knowledge]") (emphasis supplied). As the Court of Claims stated in *H.N. Bailey & Associates v. United States*, 196 Ct. Cl. 166 (1971):

> Of course, the corollary to the *Curtis* rule is that the Government is under no duty to volunteer information in its files if the contractor can reasonably be expected to seek and obtain the facts elsewhere, and this court has so held on numerous occasions. *Ambrose-Augusterfer Corp. v. United States*, 184 Ct. Cl. 18, 38 (1968); *T.F. Scholes, Inc. v. United States*, 357 F.2d 963 (1966); *National Concrete and Foundation Co. v. United States*, 170 Ct. Cl. 470, 476

(1965); *Leal v. United States*, 149 Ct. Cl. 451 (1960).

Id., 196 Ct. Cl. at 177-78.

Plaintiffs' complaint itself confirms that the subject matter of those "superior knowledge" claims is inextricably intertwined with state secrets. Plaintiffs allege that information in "other classified, special access DOD programs" was vital, not in fact disclosed by the Government, and known by the Government not to be disclosed. Second Amended Unclassified Complaint ¶¶ 46, 269-274, App. 2, 5.[5] Even though the court of appeals has made clear that this lawsuit will *not* involve "information . . . from other special access programs beyond those for which counsel have previously been granted access," *In re United States*, Misc. No. 374, slip op. at 12, plaintiffs nevertheless maintain that their claims can be meaningfully resolved in this forum. Plaintiffs' position is patently untenable.

Despite their complaint, which asserts that the unshared information was contained in special access programs, plaintiffs have recently attempted to re-characterize their superior knowledge claim as an allegation that the Government should have merely told them that it took a long time to build the B-2 and F-117A aircraft. *See* 5/25/93 Declaration of

[5] Plaintiffs would also have to establish that they could not, through reasonable diligence, have secured the allegedly vital information. *E.g., Bateson-Stolte, Inc. v. United States*, 145 Ct. Cl. 387, 392 (1959).

Keith Jackson, Jr., ¶ 7.[6] Plaintiffs' simplistic position is unlike *J.A. Jones Construction Company v. United States*, 182 Ct. Cl. 615 (1968), unlike any case that has ever been reported, and, upon a cursory examination, meaningless.

The court in *J.A. Jones* stated that a "general warning" could have discharged the Government's duty to share superior knowledge. That "general warning," however, related to the very *specific* performance problem that the plaintiff in that case encountered -- a shortage of the local labor supply. *Id.*, 182 Ct. Cl. at 618. Every "superior knowledge" case that has ever been reported has involved an allegation relating to a specific performance problem. Anything else amounts to nothing more than a general deterrent, and "it would be irresponsible procurement to seek to deter bidders from bidding, or even to seem to do so." *American Ship Building Co. v. United States*, 228 Ct. Cl. 220, 225-26 (1981).

Plaintiffs' classified appendix to their Memorandum concerning continuation of Discovery on Count IX, dated May 25, 1993, comes closer to revealing the inherent problems of their "superior knowledge" claims, and why those claims must be dismissed. Although the various manufacturing techniques and technologies there identified remain too vague to constitute "vital knowledge" for

[6] The classified and unclassified submissions we received from plaintiffs after the close of business on May 26, 1993, are factually misleading, in several significant respects. If a response is necessary for the record, we respectfully request an opportunity to submit such a clarification, in the near future.

purposes of a superior knowledge claim, they do begin to illustrate that the real complaint of plaintiffs is that they allegedly did not receive vital classified "technological information" contained in special access programs. We dispute that contention. More importantly, we dispute the notion that the complete facts here created a duty for the Government to volunteer such information, under the applicable four-part legal test for a claim of "superior knowledge." As demonstrated below, however, in this lawsuit it is not possible to determine the complete truth, *i.e.*, the respective special access information available to the parties, and any potential sources of that information.

ii. **The Facts That Would Be Required For Litigation Of Plaintiffs' Superior Knowledge Claims Are, Themselves, *State Secrets***

On multiple occasions, this Court has recognized that information that is subject to the absolute state secrets privilege constitutes "relevant information," regarding plaintiffs' superior knowledge claims. *E.g.*, 3/18/93 Order, App. 42; 5/7/93 Order, App. 49. Similarly, the Court has repeatedly determined that the privileged material is "crucial" to the resolution of plaintiffs' superior knowledge case. *E.g.*, 3/31/93 Order, App. 43; 4/12/93 Order, App. 45; 4/14/93 Order, App. 46. The court of appeals, upon its own review of the privileged information, did not dispute this Court's findings that privileged information was "crucial" and

"relevant" to resolution of plaintiffs' claims. *In re United States*, Misc. No. 374, slip op. at 18. Nevertheless, plaintiffs now represent that the Court may resolve their claims on the merits, without this indisputably "crucial" and "relevant" evidence.[7] It is clear that such a position must be rejected.

Moreover, the problems of continued litigation of plaintiffs' "superior knowledge" claims are not limited to removal of the undeniably "relevant" evidence subject to the Government's prior invocation of the state secrets privilege, but will include: (1) plaintiffs' inability to provide complete and accurate answers to our own discovery; (2) our continued inability to respond to plaintiffs' discovery; and (3) an inability of witnesses to discuss information that would be required to establish the merits of plaintiffs' claims, and the Government's defenses.

Examples of each of these problems are already before the Court. In plaintiff's Answers and Objections To Defendant's First Set of Interrogatories and First Request for Production of

[7] In response to the attempted negotiation of stipulations ordered by the Court on April 7, 1993, plaintiffs' only suggestion regarding how the parties could "avoid the need for further inquiry into sensitive areas" was for the Government to stipulate to the veracity of "superior knowledge" allegations contained in plaintiffs' complaint. Such a "suggestion essentially proves the point that the merits of this controversy are inextricably intertwined with privileged matters." *Fitzgerald v. Penthouse International, Ltd.*, 776 F.2d 1236, 1243 n.11 (4th Cir. 1985), *citing, Halkin v. Helms*, 598 F.2d 1, 10-11 (D.C. Cir. 1978).

Documents, plaintiffs generally objected because our discovery requests sought top secret and/or special access information. App. 51-54. Similarly, in plaintiffs' Answers and Objections to Defendant's Ninth Set of Interrogatories and Seventh Requests for Production of Documents, plaintiffs *specifically* declined to provide any information that would be protected within "SAR," or special access, programs. App. 56. Plaintiff's own discovery requests, including Interrogatory No. 346, and a host of interrogatories contained within Plaintiffs' Third Interrogatories and Request for Production of Documents, would be objectionable, and ultimately unanswerable, upon the same basis. In addition, as the Court is well aware, the depositions of potential witnesses in this case have already presented serious difficulties and security problems, because of inquiries directed toward plaintiffs' "superior knowledge" claims.[8]

It is a fact, and plaintiffs have readily admitted, that individuals employed by the plaintiff corporations had access to information contained in a wide array of classified, special access programs. *E.g.*, App. 59 ("Plaintiffs, in fact, during various stages of the A-12 program were granted access to various types of secret Government information, which may include some of the information at issue in this mandamus petition."). Indeed, as the

[8] Specifically, plaintiffs ' deposition of Richard Rumpf on March 11 and 12, 1993, resulted in improper, inadvertent disclosures of sensitive information. *See* 4/27/93 Order, App. 60 (subsequent retrieval of the deposition transcript, for security reasons).

attached declaration establishes, there are literally dozens and dozens of "special access" programs to which plaintiffs and their employees had access. 5/26/93 Eames Decl. ¶¶ 7, 8, App. 63.[9] If the Government reasonably believed that these plaintiffs had the means to obtain or request the technical information that they allegedly needed, there could, of course, be no breach of an implied duty by the Government to share such information. *E.g.*, *Bateson-Stolte, Inc. v. United States*, 145 Ct. Cl. at 392 (superior knowledge claim cannot be resolved if court does "not know what information the plaintiff had, or could have obtained by reasonable diligence.") (emphasis supplied). *See also H.N. Bailey & Associates*, 196 Ct. Cl. at 177-78. Because of the nature of plaintiffs' novel claims, however, the Government will not be able to explore or establish what knowledge plaintiffs may, in fact, have had, or what they reasonably could have obtained.

This point is dramatically illustrated by consideration of plaintiffs' best and final offer ("BAFO") documents, submitted to the Government during the bidding process. In those BAFO documents, plaintiffs catalogued a host of secret, special access, and even unacknowledged, programs in which they had developed knowledge and experience -- *including* programs from which they now claim the Government did not share "superior

[9] We anticipate filing a similar declaration regarding Department of the Navy programs, as an addendum to our appendix, within one or two business days.

knowledge" (*e.g.*, F-117A).[10] We are not even able to present unredacted copies of plaintiff's own documents such as these in our defense, however, because those documents include references to codewords and programs to which the trial attorneys in this litigation have not been granted access. Moreover, as demonstrated in the Government's invocation of the state secrets privilege on March 30, 1993, and in the attached declarations, this example constitutes but a glimpse of the potential problem -- there are potentially a *number* of programs, including unacknowledged or "black" programs, that might ultimately bear upon plaintiffs' wide-open superior knowledge claims, and the comprehensive Government defenses that will be necessitated by plaintiffs' open-ended allegations. 5/26/93 Eames Decl. ¶¶ 7, 8, App. 63.

The correct effect of the valid Executive access restrictions, quite simply, is to foreclose the imposition of an implied contractual *legal duty* upon the part of the Government to share compartmentalized information. *See* Part I, above. As plaintiffs admit, however, special access restrictions do not have any presumptive effect upon any *actual* sharing of technical special access information that may have occurred, or, more importantly, upon plaintiffs' *actual* opportunities to pursue such information, within the parameters of the applicable security mechanisms. Such factual matters lie at the heart of any superior knowledge

[10] *See* our Classified Appendix, Exhibits 2 and 3, filed concurrently with these motions.

claim, but cannot be resolved in this case because they depend upon information that cannot be produced in this litigation.

Plaintiffs' superior knowledge claims, therefore, present the paradigm of the situation where "'the merits . . . are inextricably intertwined with privileged matters.'" *Guong v. United States*, 860 F.2d 1063, 1066 (Fed. Cir. 1988), (*quoting Fitzgerald v. Penthouse International, Ltd.*, 776 F.2d at 1243 n.11), *cert. denied*, 490 U.S. 1023 (1989). Accordingly, litigation of plaintiffs' "superior knowledge" allegations without reference to privileged information is impossible.

B. The Authorities Require Dismissal Of Plaintiffs' Superior Knowledge Claims

The very subject matter of plaintiffs' superior knowledge claims is a state secret, and the law in this and other circuits for situations like the present is overwhelming -- plaintiffs' superior knowledge claims must be dismissed. *E.g., Guong v. United States*, 860 F.2d at 1066-67. *See also, Weinberger v. Catholic Action of Hawaii*, 454 U.S. 139, 147 (1981); *Totten v. United States*, 92 U.S. 105 (1876); *Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1141 (5th Cir. 1992), *cert. denied*, 113 S. Ct. 1843 (1993); *Bowles v. United States*, 950 F.2d 154, 156 (4th Cir. 1991); *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 547-48 (2d Cir. 1991); *Fitzgerald v. Penthouse International, Ltd.*, 776 F.2d 1236 (4th Cir. 1985); *Salisbury v. United States*, 690 F.2d 966, 977 (D.C. Cir. 1982); *Farnsworth Cannon, Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (en

banc).[11] Similarly, litigation of the claim is, of course, impossible where the plaintiff cannot establish a *prima facia* claim without reference to state secrets, or where a party's essential defense to a claim is inextricably intertwined with privileged information. *E.g., Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 547-48 (2d Cir. 1991); *Molerio v. F.B.I.*, 749 F.2d 815, 825 (D.C. Cir. 1984); *Halkin v. Helms*, 690 F.2d 977, 998-1000 (D.C. Cir. 1982) ("*Halkin II*").

Those cases where invocation of the state secrets privilege has not resulted in dismissal of the claim have either involved situations where, unlike this case, the privileged information was not inextricably intertwined with the merits, or where dismissal was not in issue. For example, in *United States v. Reynolds*, 345 U.S. 1, 11 (1953), the Supreme Court noted that the necessity for the privileged information was "dubious," and, accordingly, remanded the matter to proceed, without the evidence.[12] Likewise, *In re United States*, 872 F.2d 472, 478 (D.C. Cir. 1989), "did not present a case where 'the very subject matter of (the claim) is itself a state secret,'" and dismissal was not,

[11] As we pointed out at the hearing on May 13, 1993, plaintiffs have recognized, and successfully argued, this position in other cases, when their pecuniary interests happened to coincide with the security interests of the united States.

[12] At the same time, however, the Court reaffirmed the principal, expressed in *Totten v. United States*, 92 U.S. 105 (1875), that where the "very subject matter" of the action involves state secrets, it must be dismissed. *Reynolds*, 345 U.S. at 11 n.26.

therefore, required.[13] In *Northrop Corp. v. McDonnell Douglas Corp.*, 751 F.2d 395 (D.C. Cir. 1984), dismissal was not sought.

In this case, the authorities require that plaintiffs' "superior knowledge" claims be dismissed.

C. Sound Policies Support Dismissal Of Plaintiffs' Superior Knowledge Claims

In cases such as this, where the subject matter of a particular claim is inextricably intertwined with material and information that constitute state secrets, sound policies support dismissal of the claim. Specifically, concerns relating to the utility of the judicial process, and the necessary threat to national security that would arise from continued attempts to litigate the claim, require dismissal.

Because of the necessary invocation of the state secrets privilege, the Government's defenses, like plaintiffs' "superior knowledge" case itself, will ultimately fail to resolve: (1) whether plaintiffs actually had vital knowledge of whatever facts they

[13] In *Ellsberg v. Mitchell*, 709 F.2d 51 (D.C. Cir. 1983), *cert. denied*, 465 U.S. 1038 (1984), the court remanded the matter to the trial court, to determine whether the action could, in fact, proceed in a meaningful manner without the privileged material. The circuit court suggested that the trial court could utilize *in camera, ex parte* procedures, in making that determination. *Id.*, 709 F.2d at 69 n.78. In this case, however, it is plain that "the very subject matter" of plaintiffs' superior knowledge claims is a state secret, and additional *ex parte* procedures should not, therefore, be required. Nevertheless, if necessary, we would be willing to submit *ex parte* filings, to further demonstrate how the merits of plaintiffs' claims are inextricably intertwined with state secrets.

settle upon as constituting "superior knowledge," from other sources; (2) whether the Government was aware that the contractors had no knowledge of, or reason to obtain, the information; and (3) whether the Government, in fact, supplied the relevant information in another context, and the contractors, for competitive or other reasons, merely failed to take steps to utilize the information at their disposal. *GAF Corp. v. United States*, 932 F.2d at 949.

These questions cannot, in this proceeding, ever be fully and truthfully answered, because the Government is not able to produce evidence that would confirm or deny plaintiffs' allegations, or our defenses. In these circumstances, it is a perversion to attempt to allow the judicial process to go forward -- any efforts to resolve these issues will necessarily be an effort by one side or the other, knowingly or unknowingly, to convince the court of a falsehood. *E.g., Molerio v. F.B.I.*, 749 F.2d 815, 825 (D.C. Cir. 1984) ("mockery of justice" for the court to continue to attempt to resolve matter that inextricably involves state secrets). *See also Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 547 (2d Cir. 1991) (dismissal required where "questions [regarding merits] cannot be resolved or even put in dispute without access to [privileged information]"). The informational poverty resulting from invocation of the state secrets privilege -- which plaintiffs precipitated with their novel and unprecedented superior knowledge claims -- renders those claims nonjusticiable. *Guong v. United States*, 860 F.2d at 1066-67; *Halkin v. Helms*, 690 F.2d 977, 1000 (D.C. Cir. 1982) ("With no hope of a complete record and

adversarial development of the issue," dismissal of the claim is required.) *See also Totten v. United States*, 92 U.S. 105 (1876); *Bareford v. General Dynamics Corp.*, 973 F.2d at 1141; *Fitzgerald v. Penthouse International, Ltd.*, 776 F.2d 1236 (4th Cir. 1985).

Moreover, if the "superior knowledge" matters were to go forward, both sides would be tempted to probe closer and closer to facts that may or may not be contained in the host of possible unacknowledged programs that, if they existed, could bear upon the superior knowledge claims. Such circumstances (which have already occurred -- *see* 4/27/93 Order, App. 60) pose additional dangers to national security, even if strictly privileged matters are not directly disclosed.[14] Accordingly, dismissal is required. *E.g.*, *Fitzgerald v. Penthouse Int'l, Ltd.*, 776 F.2d 1236, 1243 (4th Cir. 1985) (dismissal appropriate because

[14] For example, plaintiffs may eventually point to a particular technology from the B-2 program as allegedly "superior knowledge" that was not shared from that program. It is probable, however, that the particular technology was, in fact, available to plaintiffs from one of any number of other special access, possibly covert programs, which are too sensitive to be made a part of this lawsuit. *See* 5/26/93 Eames Decl. ¶¶ 7, 8, App. 63. Witnesses with knowledge of those matters, however, will be placed in extraordinarily difficult situations during direct and cross examination, as attorneys from both sides, knowingly or unknowingly, try to focus upon the secret and possibly covert matters. That has already occurred in the deposition of Richard Rumpf, in early March of this year. National security will continue to be jeopardized in this way, through continued litigation of plaintiffs' superior knowledge claims.

"the parties would have every incentive to probe dangerously close to state secrets themselves"); *Farnsworth Cannon, Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (en banc). *See also Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1143 (5th cir. 1992); *Bowles v. United States*, 950 F.2d 154, 156 (4th Cir. 1991).

For these reasons, even if plaintiffs could point to circumstances that would, taken in isolation, establish a *prima facia* case for breach of the implied duty to share superior knowledge, it is not appropriate to continue to attempt to litigate the matters. The Government would be precluded from pointing to dispositive responses to plaintiffs' superficial showings, and both sides would attempt to probe closer and closer to privileged matters. Dismissal of the claims is, therefore, required. *E.g.*, *Fitzgerald v. Penthouse International, Ltd.*, 776 F.2d 1236 (4th Cir. 1985); *Farnsworth Cannon, Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (en banc). *See also Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1143 (5th Cir. 1992). In sum, because the very subject matter of plaintiffs' superior knowledge claims, and the Government's defenses to those claims, involve state secrets, those claims must be dismissed. Dismissal is supported by the overwhelming weight of authority, sound policies, and fundamental conceptions that underlie the legitimacy of the judicial process.

IV. Plaintiffs Are Not Entitled To Any Judgments, Findings, Or Dispositions In Their Favor, Simply Because They Have Forced The Government To Invoke The State Secrets Privilege

Plaintiffs have previously indicated an intent to argue that if they necessitate an invocation of the state secrets privilege, and thereby eliminate their "defense" of "superior knowledge," they are nevertheless entitled to findings, or a judgment, in their favor. For a variety of fundamental legal and logical reasons, however, such misdirected arguments must be rejected.

Specifically: (1) the authorities conclusively establish that no adverse impact may be drawn against the Government for invocation of the privilege; (2) if an adverse inference against the Government were drawn in these circumstances, the Government's ability to terminate defense contractors for default would effectively be eliminated -- which *cannot* be the case; and (3) because the "very subject matter" of the default termination does not involve state secrets, invocation of the privilege does not prohibit the Government from establishing plaintiffs' default.

First, it is beyond dispute that no adverse inference may be drawn against the Government merely for invoking the privilege in a matter in which the Government is a party -- it is well established that the effect of the privilege is the "same," whether or not the Government is a party to the litigation. *E.g.*, *In re United States*, 872 F.2d at

476 ("Notions of sovereign immunity preclude . . . adverse consequence to the government, such as alteration of procedural or substantive rules"), *citing*, *Ellsberg*, 709 F.2d at 65 ("the effect is the same, in other words, as if the government were not involved in the controversy"); *Salisbury v. United States*, 690 F.2d 966, 976 (D.C. Cir. 1982); *Pan American World Airways, Inc. v. Aetna Casualty & Surety Co.*, 368 F. Supp. 1098, 1139 (S.D.N.Y. 1973), *aff'd*, 505 F.2d 989 (2d Cir. 1974); *Sigler v. LeVan*, 485 F. Supp. 28 185, 192-95 (D. Md. 1980); *Kinoy v. Mitchell*, 67 F.R.D. 1, 15 n.50 (S.D.N.Y. 1975).[15]

[15] It is true that extraneous concerns make it inappropriate in some circumstances for the Government to proceed criminally against an individual, and simultaneously to invoke the state secrets privilege. *E.g.*, *United States v. Lopez*, 328 F. Supp. 1077, 1089 (E.D.N.Y. 1971). *Cf.* 18 U.S.C. App. IV § 1 *et. seq.* Allegations that the same rationale should broadly apply to a civil case such as this, *cf.*, *McCormick on Evidence* § 109 (Edward W. Cleary ed. 1984), are not sound. First, the Supreme Court has unequivocally stated that the rationale from the criminal cases "has no application in a civil forum where the Government is not the moving party, but is a defendant only on terms to which it has consented. In *Reynolds*, 345 U.S. at 12. Second, this lawsuit, in a forum for resolving civil contractual disputes, necessarily involves the "notions of sovereign immunity" that prevent the imposition of special sanctions against the Government, for invoking the state secrets privilege. *In re United States*, 872 F.2d at 476; *Ellsberg*, 709 F.2d at 65; *Salisbury*, 690 F. 2d at 976. Indeed, the forced invocation of the state secrets privilege is, essentially, a sovereign act. It is fundamental, of course, that the Government cannot be held contractually liable for acts that it takes, as a sovereign. *E.g.*, *Horowitz v. United States*, 267 U.S. 458, 461 (1924); *Atlas Corp. v. United States*, 895 F.2d 745, 754 (Fed. Cir. 1990).

As the court stated in *Attorney General v. Irish People, Inc.*, 684 F.2d 928, 931 (D.C. Cir. 1982), *cert. denied*, 459 U.S. 1172 (1983), "outright dismissal [of the Government's civil claim] may be too extreme a measure to invoke for [the Government's] inability to comply with defendant's discovery request." In addition to cautioning generally against punishing the Government-as-litigant when invocation of the state secrets privilege is necessary, the court in *Irish People* described several factors that should be considered before dismissal of any claim by the Government -- *all* of those factors proscribe the imposition of any sanction against the Government in this case. *Id.* 684 F.2d at 951.[16]

[16] Specifically, the privileged information is not likely to exculpate plaintiffs -- the nature of the privileged information, in fact, includes matters that could provide a complete defense *for the Government* to plaintiffs' "superior knowledge" claims. Plaintiffs have no overriding necessity for their attenuated, ancillary excuse of "superior knowledge," nor is the loss of a single, legally-deficient excuse fatal to plaintiffs' ability to present their position concerning their A-12 performance failure. The Government's interest in maintaining the secrecy of its most valuable military secrets, and in successfully retaining the ability to terminate non-performing military contractors, is paramount. In attempting to allow plaintiffs to develop their legally baseless "superior knowledge" excuse until it became apparent that that would not be possible, the Government has exhibited extraordinary cooperation. Rather than sanctioning the Government for protecting national security, this case could simply become focused upon what should be at issue, namely plaintiffs' performance failures under the A-12 contract. *Irish People*, 684 F.2d at 951.

Second, common sense demands the rejection of any assertion by plaintiffs that the elimination of their novel "superior knowledge" claims should somehow preclude the Government from prevailing upon the entire default termination. Pursuant to such a view, *every* terminated defense contractor could make a claim that the Government failed to share information contained in secret, unacknowledged programs. The Government would then be forced either to disclose the existence and substance of the programs to defend itself, or lose its ability to terminate contractors for default. That, of course, is a preposterous proposition, and cannot be the law. The Government's ability to insist upon performance of contracts for the procurement of defense-related goods and services would be eviscerated. Moreover, such a view would eliminate the ability of the Executive to control access to military and diplomatic matters, in clear violation of constitutional proscriptions, *e.g.*, *Department of the Navy v. Egan*, 484 U.S. 518, 527-28 (1988), and would impose an automatic penalty upon the Government for invoking the state secrets privilege, in violation of settled principals. *E.g.*, *In re United States*, 872 F.2d at 476; *Ellsberg*, 709 F.2d at 65.

Third, elimination of plaintiffs' superior knowledge claims does not, of course, mean that the Court cannot adjudicate the entire default termination itself. Dismissal is, admittedly, a "drastic remedy," *cf. Fitzgerald v. Penthouse Int'l, Ltd.*, 776 F.2d 1236, 1242 (4th Cir. 1985), and should be imposed only to the extent necessary, where no other alternative is possible. Merely because

plaintiffs have purported to tie their defense to a non-justiciable, attenuated claim of superior knowledge, they cannot insulate themselves from their failure to perform this A-12 contract. Plaintiffs are not precluded from defending against the default termination claim here -- they are only foreclosed, properly, from pursuing their ancillary claim that the Government breached an implied contractual duty to share secret, classified "superior knowledge." That superior knowledge claim, because it is inextricably intertwined with state secrets, cannot be litigated, and must be dismissed.

V. The Court Should Enter A Protective Order Prohibiting All "Superior Knowledge" Discovery

Further discovery relating to plaintiffs' "superior knowledge" claims should not be allowed. Such discovery will be directed toward a claim that must be dismissed, and will therefore not reasonably be calculated to lead to relevant or admissible evidence. More importantly, such discovery will needlessly endanger national security, for no legitimate purpose.

As demonstrated above, plaintiffs' "superior knowledge" claims must, ultimately, be dismissed. It is fundamental that "[d]iscovery may not be had regarding a matter which is not 'relevant to the subject matter involved in the pending action.'" *Micro Motion, Inc. v. Kane Steel Co.*, Inc, 894 F.2d 1318, 1323 (Fed. Cir. 1990), *quoting* Fed. R. Civ. Proc. 26(b)(1). The superior knowledge claims should

not remain "pending" before this Court, and further discovery should be disallowed upon that basis.[17]

Moreover, this case is exactly like *Molerio v. F.B.I.*, 749 F.2d 815 (D.C. Cir. 1984), *Bareford v. General Dynamics Corp.*, 973 F.2d 1138 (5th Cir. 1992), *cert. denied*, 113 S. Ct. 1843 (1993), and, particularly, *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544 (2d Cir. 1991), where the courts held that ongoing activities purportedly in pursuit of a claim that was inextricably intertwined with state secrets were not permissible. As in *Zuckerbraun*, 935 F.2d at 548, "[d]iscovery would thus be a waste of time and resources."

Because further inquiry would "inevitably lead to a significant risk" of disclosure of national secrets, *Bareford v. General Dynamics Corp.*, 973 F. 2d at 1144, continued discovery regarding plaintiffs' "superior knowledge" claims is not appropriate here.

The attempted imposition of an implied contractual duty to share classified, compartmentalized information in this case violates fundamental constitutional principles underlying Executive control of access to such information. *E.g.*,

[17] During the pendency of this dispositive motion, discovery should be precluded. *E.g.*, *Harlow v. Fitzgerald*, 457 U.S. 800, 817-18 (1982); *Florsheim Shoe Co., Div. of Interco, Inc. v. United States*, 744 F.2d 787, 797 (Fed. Cir. 1984); *Reliance Ins. Co. v. United States*, 18 Cl. Ct. 359, 360-61 (1989); *Coastal Gas Corp. v. Department of Energy*, 84 F.R.D. 278, 282 (D. Del. 1979) (staying discovery pending resolution of dispositive motion is an "eminently logical means to prevent wasting the time and effort of all concerned, and to make the most efficient use of judicial resources.")

Department of the Navy v. Egan, 484 U.S. 518, 527-28 (1988). In the Tucker and Contract Disputes Acts, Congress allowed the Government to be sued on certain contractual claims, and so waived sovereign immunity for those purposes. However, for constitutional reasons, Congress did not, and could not, "abrogate the state secrets privilege of the Executive." *Salisbury v. United States*, 690 F.2d 966, 975 (D.C. Cir. 1982), *citing*, *Black v. Sheraton Corp. of America*, 564 F.2d 531, 541 (D.C. Cir. 1977). *See also American Tel. & Tel. v. United States*, 4 Cl. Ct. 147, 160 (1983). Plaintiffs' "superior knowledge" claims should have been dismissed because they are legally deficient; they have now, unavoidably, resulted in invocation of the state secrets privilege, and must be dismissed for that reason.

CONCLUSION

For the reasons stated above, we respectfully request that the Court: (1) dismiss plaintiffs' "superior knowledge" claims; and (2) issue a permanent protective order prohibiting attempted discovery into other classified, special access programs.

Respectfully submitted,

STUART E. SCHIFFER
Acting Assistant
Attorney General

/s/DAVID M. COHEN
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May 27, 1993

Attorneys for Defendant

In the United States Court of Federal Claims

No. 91-1204C

(Filed: June 21, 1993)

McDONNELL DOUGLAS CORPORATION AND GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	State secrets doctrine; Effect on Defendant's case; Standards for Dismissal.
v.	)	
UNITED STATES OF AMERICA.	)	
Defendant.	)	

Francis M. Gaffney, St. Louis, Missouri, attorney for plaintiff McDonnell Douglas Corporation and, *Herbert L. Fenster*, Washington, D.C., attorney for plaintiff General Dynamics Corporation.

Mary Mitchelson, United States Department of Justice, Washington, D.C., for defendant.

OPINION AND ORDER

Defendant moved for dismissal of plaintiffs' superior knowledge claims on the basis that secret information unavailable to plaintiffs is "inextricably intertwined" with the merits of those claims.

Dismissal would be appropriate in these circumstances if trial could result in an unacceptable risk to national security[1] or impermissible prejudice to defendant.[2] Defendant's classified *in camera* appendix does not make such a showing.

In response to court order, plaintiffs made an impressive showing that they can present a prima facie case under the existing discovery restrictions imposed by defendant. The unavailability of certain information does not require dismissal because plaintiffs have shown that they can proceed with the information available. *See, e.g., Ellsberg v. Mitchell*, 709 F.2d 51, 65 (D.C. Cir. 1983), *cert. denied*, 465 U.S. 1038 (1984). Defendant therefore seeks dismissal on the basis that information needed to rebut plaintiffs' prima facie case will remain unavailable due to national security concerns. That is, the United States now argues that its defense of this case will be hampered by its own classification and special access procedures.[3]

[1] *See, e.g., Farnsworth Cannon, Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (en banc); *Halpern v. United States*, 258 F.2d 36, 44 (2nd Cir. 1958). Defendant points out that discovery already has resulted in improper disclosures of sensitive information. However, defendant is aware that responsibility for this disclosure cannot be placed upon plaintiffs.

[2] *See Molerio v. F.B.I.*, 749 F.2d 815, 825 (D.C. Cir. 1984).

[3] This is an odd notion as stated, but one supported by case law for certain policy reasons. *See, e.g., In re United States*, 872 F.2d 472,476-77 (D.C. Cir.), *cert. denied*, 493 U.S. 960 (1989);

In support of this assertion defendant points to invocation of the state secrets doctrine by Acting Secretary Donley, and other *in camera* declarations. We are not convinced that these submissions clearly establish that dismissal is warranted. Evidence submitted by a plaintiff's employee may suggest otherwise-or at least raise a substantial question which defendant has not addressed. In *Molerio,* the *in camera* affidavit "specifically set forth [the Government's defense]." 749 F.2d at 822. Dismissal was appropriate because the Government's showing was conclusive. *Molerio,* 749 F.2d at 825.

In asking for dismissal, defendant invites a harsh result. This is particularly so because plaintiffs' counsel cannot participate fully in this issue even though the result could be a multibillion dollar judgment against their clients. Defendant must establish clearly that its invocation of the state secrets doctrine precludes it from proving at trial facts vital to its defense.

Counsel for defendant also asserts emphatically that national security concerns will preclude access to a large number of sources of information which may be critical to ascertaining the truth in this case. We do not doubt this assertion, but it lacks necessary support. Defendant has made such a showing in other cases. *See Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 548-52 (2nd Cir. 1991) (declaration of Secretary of the Navy

Ellsberg v. Mitchell, 709 F.2d 51, 64 (D.C. Cir. 1983), *cert. denied,* 465 U.S. 1038 (1984).

Garrett). We see no reason why defendant cannot do the same here. Invocation of the state secrets doctrine by the appropriate official in the Department of Defense to withhold the information to which counsel alludes may be the proper approach. Such a showing may avoid the need for further *in camera, ex parte* procedures.

We stayed discovery of Count IX pending a showing that plaintiffs could establish a prima facie case under the conditions imposed by defendant. Plaintiffs satisfied that condition. We propose to lift the stay unless defendant intends to address our concerns on the *Molerio* issue or to invoke the state secrets doctrine to preclude trial of plaintiffs' superior knowledge claims. Defendant will respond by noon on June 24, 1993 whether it intends to take further action on this issue.

Defendant's motion to dismiss, or in the alternative, for partial summary judgment, is CONTINUED.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DEFENDANT'S SUPPLEMENT TO MOTION TO DISMISS PLAINTIFFS' "SUPERIOR KNOWLEDGE" CLAIMS

On May 27, 1993, following the invocation of the military and state secrets privilege in this action by the Acting Secretary of the Air Force, and the ruling by the United States Court of Appeals for the Federal Circuit sustaining that invocation, the Government moved to dismiss plaintiffs' "superior knowledge" claims, upon the basis that "'the merits [of plaintiffs' claims] are inextricably intertwined with privileged matters.'" *Guong v. United States*, 860 F.2d 1063, 1066 (Fed. Cir. 1988), (*quoting Fitzgerald v. Penthouse International. Ltd.*, 776 F.2d at 1243 n. 11), *cert. denied*, 490 U.S. 1023 (1989). *See also Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544 (2d Cir. 1991), *Bareford v. General*

Dynamics Corp., 973 F.2d 1138 (5th Cir. 1992), *cert. denied*, 113 S. Ct. 1843 (1993).

On June 21, 1993, the Court issued an opinion and order, wherein it continued our motion. The Court indicated that it would consider the matter further, if the Government made further showings regarding how invocation of the absolute state secrets privilege in this case would "preclude trial of plaintiffs' superior knowledge claims." 6/21/93 Order at 3. The court cited *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544 (2d Cir. 1991), as an example of a public declaration in support of invocation of the military state secrets privilege that necessitated dismissal of claims dependent upon privileged material.[1]

[1] The Court has also referred to *Molerio v. F.B.I.*, 749 F.2d 815 (D.C. Cir. 1984), wherein the appellate court indicated that its own review of privileged materials convinced it that the plaintiff in that case could not prevail upon his claim. In the unique, current posture of this case, *i.e.* with the persistent unwillingness or inability of plaintiffs to identify precisely what "superior knowledge" they allege should have been shared, the previously-submitted materials relating to the prior invocation of the military state secrets provide the most comprehensive "*Molerio* showing" presently possible. We respectfully submit that those materials conclusively demonstrate that the Court cannot resolve each of the elements of plaintiffs' "superior knowledge" claims without reference to privileged information. Plaintiffs' claims, therefore, must be dismissed; continued pursuit of those claims would amount to nothing more than the "mockery of justice" deemed impermissible by the *Molerio* court. *Id.*, 749 F.2d at 825.

In *Zuckerbraun*, then-Secretary of the Navy H. Lawrence Garrett III submitted a public declaration that: (1) described his understanding and review of the subject matter of certain claims; (2) described the classified aspects of the information that would be required to resolve those claims; and (3) conveyed his conclusion that trial of those matters would unavoidably call for information which is classified, and subject to the military state secrets privilege. *Id.*, 935 F.2d at 548-553.

Attached is a declaration by the current Acting Secretary of the Air Force, Merrill A. McPeak. As that declaration and our prior submissions establish, this case, like *Zuckerbraun* and *Bareford*, presents circumstances that require dismissal of plaintiffs' claims, because any further efforts to litigate those claims "would threaten disclosure of important state secrets." *Bareford*, 973 F.2d at 1143, *citing*, *Bowles v. United States*, 950 F.2d 154, 156 (4th Cir. 1991); *Fitzgerald v. Penthouse International, Ltd.*, 776 F.2d 1236 (4th Cir. 1985); *Farnsworth Cannon. Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (en banc). In *Zuckerbraun* and *Bareford*, the plaintiffs argued that they could avoid implicating privileged information in their pursuit of tort actions against manufacturers of certain weapons systems. Declarations by the Secretary of the Navy established that those plaintiffs could not attempt to artificially tailor their claims to avoid privileged matters and, accordingly, the courts of appeal affirmed dismissals of both actions.

In this case, the very nature of plaintiffs' "superior knowledge" claims is even more "inextricably intertwined" with privileged matters than the negligence claims of the *Bareford* and *Zuckerbraun* plaintiffs.[2] As the Acting Secretary of the Air Force has conclusively and unequivocally stated, "[t]he development of evidence on these matters during the course of discovery and presentation of that evidence during trial unavoidably will call for information which I have determined cannot be disclosed, consistent with safeguarding national security." McPeak Decl. ¶ 13. Acting Secretaries of the Air Force Donley and McPeak, like former Secretary of the Navy Garrett in the *Bareford* and *Zuckerbraun* cases, have personally determined that "the development of evidence during the course of discovery and presentation of that information at trial unavoidably will call for information which is classified," and which cannot be disclosed without impermissibly endangering national security. *Zuckerbraun*, 935 F.2d at 552.

For these reasons, and for the additional reasons set forth in our prior pleadings, plaintiffs' "superior knowledge" claims must be dismissed.

Respectfully submitted,

FRANK W. HUNGER

[2] Indeed, plaintiffs' very complaint in this case confirms the classified, special access-required nature of the information upon which their claims are based. *See* Second Amended Unclassified Complaint ¶¶ 46-47, 55-59, 269-274.

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July 23, 1993

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DECLARATION OF THE ACTING SECRETARY OF THE AIR FORCE MERRILL A. McPEAK

I, Merrill A. McPeak, declare:

1. I am the Acting Secretary of the Air Force. As such, I am currently the head of the Department of the Air Force. I am responsible for, and have the authority necessary to conduct, all affairs of the Department of the Air Force. I am also presently responsible for the formulation of policies and programs by the Department of the Air Force that are fully consistent with national security objectives and policies established by the President and the Secretary of Defense.

2. In my capacity as chief executive officer of the Air Force, I possess original classification authority, and am authorized by the

President under Executive Order 12356 to determine the proper classification of information, and, consistent with that Executive Order, to create compartmentalized, or "special access," programs in order to further safeguard against the unauthorized disclosure of militarily sensitive information.

3. On March 30, 1993, former Acting Secretary of the Air Force Michael B. Donley invoked the military and state secrets privilege, with respect to matters that were relevant to certain claims in this litigation. Acting Secretary Donley concluded that the threat of exceptionally grave damage to national security prohibited the disclosure of those matters for purposes of this litigation, and, accordingly, formally invoked the military and state secrets privilege. Acting Secretary Donley also indicated that, to the extent that litigation of plaintiffs' claims presented a continuing need for release of classified, special access information related to low observable technology, he would continue to view his responsibility to protect the national security as requiring invocation of the military and state secrets privilege.

4. I have reviewed the determinations of Acting Secretary Donley regarding his invocation of the military and state secrets privilege, and I concur completely in his assessments and judgments on those matters.

5. The purpose of this declaration is to describe the threat of unauthorized disclosure of information for which Acting Secretary Donley has asserted the military and state secrets privilege, and, further, to describe the nature and classification of the additional information that will be required, if this litigation continues to involve Air Force special access programs. For the reasons set forth below, I have concluded that continued inquiry into what is known as plaintiffs' "superior knowledge" claims would necessarily require examination and use of information that cannot be disclosed in this litigation. Those "superior knowledge" claims necessarily implicate highly classified sources, origins and derivations of various low observable technologies. Litigation of plaintiffs' "superior knowledge" claims would present a continuing threat of disclosure of information for which the military and state secrets privilege has been asserted, and would present a need for disclosure of additional information over which I would assert the privilege.

6. The statements in this declaration are based upon my personal review and consideration of these matters. I have reviewed various pleadings, which contain allegations regarding the Government's alleged duty to share its "superior knowledge" of information classified as special access required, pursuant to Executive Order 12356. I have also reviewed court orders in this action. In addition, I have been advised of the inquiry that would be required for litigation of

plaintiffs' "superior knowledge" claims, and, more particularly, the Government's defenses to those claims.

7. I have been advised that the nature of plaintiffs' "superior knowledge" claims and the Government's factual defenses to those claims will involve inquiry into questions such as:

a. Whether plaintiffs actually possessed information relating to design and production of low observable aircraft or weapons systems, reasonable access to such information, or any means of obtaining such information;

b. Whether the Government was aware that plaintiffs had no knowledge of, or reasonable access to, information relating to design and production of low observable aircraft or weapons systems;

c. Whether there were mechanisms, methods, procedures, or other means by which plaintiffs could have obtained information relating to design and production of low observable aircraft or weapons systems; and

d. Whether the Government, in fact, supplied vital information relating to design and production of low observable aircraft or weapons systems to one or

both of these plaintiffs, in some context, or through some manner or means.

8. Information that would be required for litigation of plaintiffs' "superior knowledge" allegations would include technological data related to weight, profile or signature, and materials involved in design and construction of "stealth," or low observable, aircraft and weapons systems. More specifically, required information would include matters relating to composite layup; composite fabrication, processing, and stiffening; low observable characteristics of external surfaces and discontinuities; radar absorbing materials and radar absorbing structures; surface shaping; integration of subsystems; low observable finishes and paints; infrared, acoustic, visual and electromagnetic emissions with respect to various technologies and materials; and performance requirements and specifications for other low observable weapons systems and aircraft. I conclude that disclosure of the required information would cause exceptionally grave damage to national security.

9. I have considered carefully the classified aspects of the above-described information and materials, as well as the information and materials subject to the prior invocation of the military state secrets privilege. As described more fully in Acting Secretary Donley's prior declarations, the disclosure of classified information related to these matters would cause exceptionally grave damage to

national security, and, accordingly, the military and state secrets privilege was invoked with regard to certain matters on March 30, 1993.

10. My review of the inquiry which must be made into plaintiffs' "superior knowledge" claims convinces me that they involve matters that cannot be disclosed in this litigation. For example, the Government would not be able to provide complete answers to the many questions raised (as described in paragraph 7 above) because such responses would implicate matters for which the military state secrets privilege applies. Relatively straightforward questions concerning plaintiff's "superior knowledge" claims asked in depositions, or at trial, would pose unacceptable risks of disclosure of classified, special access information to individuals not authorized to receive such information. I am informed that such incidents have already occurred during pre-trial discovery, despite the apparent good faith efforts of all concerned during the deposition sessions.

11. I have been advised of the contention that plaintiffs' "superior knowledge" claims could proceed without the necessity for unauthorized disclosure of classified, special access required information, under the theory that the Government could have provided an unclassified "general warning" derived from the classified and special access information that plaintiffs allege the Government failed to share. The nature of the classified technological information upon which plaintiffs' "superior knowledge" claims are based,

however, cannot be distilled into an unclassified "general warning," consistent with security safeguards imposed by Executive Order 12356 and the applicable program security guides. As described more fully in Acting Secretary Donley's March 30, 1993 invocation of the military and state secrets privilege, special access programs may be acknowledged (overt) or unacknowledged (covert) in nature. The mere existence of an unacknowledged program is classified within the boundaries of the special access program. That is, one must be approved for access before one may know that the program exists at all. Therefore, acceptable methods for sharing or transmitting special access required information would not include unclassified "general warnings" based upon information contained in an unacknowledged special access program. This is so because the very existence of the program, and the source and nature of the information contained in the program, could not be disclosed.

12. Litigation of plaintiffs' "superior knowledge" claims will unavoidably call for low observable technological information, and sources, origins, and derivations of that information, either directly or by a process of elimination. Even if the parties attempted to exclude requests for classified special access information, or attempted to limit the "superior knowledge" claims and defenses to unclassified programs or "unclassified general warning" theories, I believe that there is a

substantial risk that classified, special access information would be disclosed inadvertently.

13. Plaintiffs' "superior knowledge" claims are predicated upon the sharing and exchange of classified, special access information related to low observable weapons systems and technology. The development of evidence on these matters during the course of discovery and presentation of that evidence during trial unavoidably will call for information which I have determined cannot be disclosed, consistent with safeguarding national security.

14. I declare under penalty of perjury that the forgoing statements are true and correct to the best of my knowledge, information and belief.

/s/ Merrill A. McPeak
Merrill A. McPeak
Acting Secretary of the Air Force

Executed this 22 day of July, 1993.

CERTIFICATE OF SERVICE

I certify under penalty of perjury that on July 23, 1993, I caused to be served a copy of "DEFENDANT'S SUPPLEMENT TO MOTION TO DISMISS PLAINTIFFS' "SUPERIOR KNOWLEDGE" CLAIMS," (1) by express courier (Federal Express Courier), addressed as follows:

Francis M. Gaffney, Esq.
SONNENSCHEIN, NATH
& ROSENTHAL
1 Metropolitan Square,
#3000
St. Louis, MO 63102

and (2) by hand-delivery, addressed as follows:

Herbert L. Fenster, Esq.
McKENNA & CUNEO
1575 Eye St., N.W., #800
Washington, D.C. 20005

/s/

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
	)	No. 91-1204C
Plaintiffs,	)	
	)	Filed: August 11, 1993
v.	)	
	)	
UNITED STATES OF AMERICA,	)	
	)	
Defendant.	)	

ORDER

General McPeak did not invoke the state secrets privilege over the matters discussed in his July 22, 1993 declaration. The declaration nevertheless includes assertions of risk to national security that we cannot ignore. We have concluded that further inquiry poses an unacceptable risk. Discovery already has resulted in improper disclosures, despite the participation of knowledgeable government officials.

We rule that plaintiffs' superior knowledge claims cannot be litigated for reasons stated in the declaration of General McPeak, and for other reasons made apparent to this court through prior *in camera*

submissions related to defendant's invocation of the state secrets privilege. This does not mean that plaintiffs' superior knowledge claims should be dismissed; we express no opinion on the legal result of this ruling. That issue would be a matter for counsel to argue at a later date.

All discovery of defendant's superior knowledge is terminated. Counsel will propose a schedule to address the legal effect of this Order.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DECLARATION OF ALBERT P. FARR III(U)

I, Albert P. Farr III, hereby declare as follows:

1. (U) I have been employed by McDonnell Aircraft Company ("MCAIR") since July 1967. My current position at MCAIR is A-12 Program Manager and Director, A-12 Program Engineering. In addition to my work on the A-12, I previously directed the Advanced F/A-18 program (developing derivatives of the original F/A-18), served as Chief Engineer for the propulsion and thermodynamics department, and have worked on the F/A-18, the AV-8B, and the F-15 programs in various capacities.

2. (U) My professional field is aerospace engineering. I received a BS in mechanical engineering from the University of Texas, an MS in mechanical engineering from the University of Southern California, and an MBA from Washington University in St. Louis.

3. (U) I was chief of Advanced Tactical Aircraft ("ATA") Engineering at MCAIR from March 1986 to September 1986. In that capacity, I was jointly responsible with Keith Jackson, my counterpart at General Dynamics, Fort Worth ("GDFW"), for all engineering analysis, design, and testing for the ATA program. Since September 1986, I have been Director, ATA Engineering (which became "A-12 Engineering" after the ATA was designated the A-12). As Director of Engineering for the MCAIR portion of the A-12 pre-contract Demonstration/Validation ("Dem/Val") phase (June 1986 to November 1987) as well as for the Full Scale Engineering Development program ("FSED") (January 1988 to termination), I was responsible for all analysis, design, development, and testing of the A-12, and was leader of the multi-disciplined development teams which designed and procured all elements of the A-12 weapons system, airframe, and associated equipment for which MCAIR had responsibility.

4. (U) I have personal knowledge of the facts set forth herein and, if called as a witness, I could

and would competently testify thereto, under oath.

5. [REDACTED] The purpose of this declaration is to provide a summary of the information relevant to the Contractors' superior knowledge claims. This document describes the three principal areas -- weight, LO suite development, and manufacturing/materials experience -- in which the Contractors lacked vital superior knowledge information to successfully conduct the A-12 FSED program. The experience level of MCAIR in [REDACTED] is described and documented, as are the Contractors' efforts to obtain the needed data. Finally, the declaration discusses the details of the three areas of superior knowledge information, and the effects of not receiving this information from the government. For completeness, some of the information herein has been provided in my previous declarations submitted to the Court; additional facts and supporting documentation relevant to superior knowledge are also provided in this declaration.

A. (U) Three Areas of Superior Knowledge

6. (U) The United States has developed the B-2 bomber and the F-117 fighter. Both aircraft make extensive use of stealth or low observable ("LO") technologies. Technological advances incorporated in the B-2 and F-117 programs would have provided very

substantial assistance to the development program for the A-12.

7. (U) The B-2 experience in particular was vital to the A-12 team because it is quite similar to the A-12. Like the A-12, the B-2 is a flying wing shape which makes extensive use of large composite structures[1], supporting a thick-wing (that is, a relatively large amount of space between the upper and lower wing surfaces) design with internal weapons bays and with imbedded engines, including inlets and exhausts. Furthermore, the B-2, the F-117 and the A-12 are all subsonic (in contrast to supersonic) non-afterburning aircraft which operate in the same flight regimes and would encounter the same enemy threats. Moreover, both the B-2 and the F-117 programs were significantly farther along in development than the A-12. In fact, the B-2 was rolled out for public view in 1988 and is currently in flight testing, and the F-117 was an operational aircraft in 1983.

[1] (U) Composite structures, in contrast to conventional structures made of metal, such as aluminum and titanium, are made of carbon fiber material that uses a resin to bind the fibers together. Once a number of plies (or sheets) of the carbon fiber materials are stacked in a certain arrangement and put in an autoclave (which is like a pressure cooker) at elevated temperature and pressure for a certain period of time, the resin liquifies and flows through the fibers binding them together into a "composite" part. Among other benefits, composite parts are lighter than metal and are used to reduce aircraft weight.

8. [REDACTED] In mid 1986 the Navy distributed its "ATA Acquisition Strategy" to MCAIR and GDFW. The Acquisition Strategy provided that:

> To take advantage of previous technologies developed by the USAF and to minimize life cycle costs, the Navy and the Air Force were directed to form a joint committee to minimize duplication of development efforts on the ATA and the USAF Advanced Tactical Fighter (ATF).

(ATA Acquisition Strategy, Ex. 2 to Motion for Summary Judgment on Count IX, NAVAIR document 201/BRR/0180-86 dated 7/12/86.)

9. [REDACTED] Further, MCAIR received the Navy's Operational Requirements (OR) for the ATA as an attachment to the Navy Request for Proposal dated December 19, 1986. The OR stated:

> The ATA shall use, to the maximum extent, [REDACTED] technology being developed on similar inter and intraservice programs and shall incorporate those weapons and expendables that are being developed for use in a [REDACTED] environment.

(ATA Operational Requirements, Ex. 3 to Motion for Summary Judgment on Count IX

NAVAIR document 201/BRR/0403-86, 12/5/86, paragraph 8.) The Contractors relied on the provisions of the OR and assumed that the ATA program would have information available from or incorporate LO technologies developed on other weapons system programs.

10. (U) The information that the Contractors needed from the B-2 and F-117 programs fell into three principal categories: weight, LO suite[2] development, and manufacturing /materials experience.

11. (U) Prior to contract award, access to B-2 and F-117 information would have altered the weight, performance, cost, and schedule estimates contained in the Contractors' proposal. Because the government did not indicate otherwise, Plaintiffs believed that the A-12 program risks had been reduced so that the aircraft could be developed within the stated fixed price, schedule and specifications.

12. (U) After contract award, the government's superior knowledge, if provided on a timely basis, would have saved the Contractors from "reinventing the wheel." Based upon the B-2 and F-117 briefings that I received during the

[2] (U) The LO suite is composed of radar absorbing materials, radar absorbing structures, surface shaping, finishes and paints, integration, and other treatments that result in low radar cross section, infrared, acoustic, visual and electromagnetic emissions levels (and, hence decreased detectability) for the aircraft.

A-12 program, and on review of B-2 and F-117 documents which has been conducted in connection with this litigation, vital information was available in several areas, including weight reduction, LO suite development, and manufacture of large composite parts; the Contractors incurred substantial delay and expense as they sought solutions to these problems that were addressed on the B-2 and F-117.

13. (U) Weight has a very significant effect on aircraft performance; an increase in weight affects important performance items such as carrier takeoff and landing speeds (so called, wind-over-deck requirements), payload (how many pounds of weapons the airplane can carry), and range (how far the airplane can go from the carrier to a target). The Contractors' initial weight estimates for the A-12 were low due to the lack of vital information, such as B-2 and F-117 weight experience, in the Contractors' weight estimating data bases. This information, if provided by the government, would have been incorporated into the Contractors' data bases and would have provided a more accurate weight estimate. Access to B-2 and F-117 weight data, including specifically weight histories, weight trade studies and structural and LO suite weight growth, would have significantly aided the Contractors in dealing with the A-12's weight, cost and schedule increases.

14. (U) The second area where information from other classified programs was vital to the performance of the A-12 FSED contract was in the development of low observables. An aircraft may be detected by an enemy in several ways - by radar, heat sensing devices, sound, sight, and by detection of the electromagnetic waves that are emitted by the airplane's electrical devices such as radios, computers, navigation equipment (collectively termed the "avionics suite"). From the perspective of low observability then, an aircraft is said to have various relevant signature characteristics: its radar cross section ("RCS"), infrared ("IR"), acoustic, visual and electro-magnetic emissions. Disguising the aircraft to reduce detectability by the enemy in each of these areas is the task of low observability. In fact, low observability was a primary requirement for the development of the A- 12.

15. [REDACTED] The third area where information vital to the A-12 was available from other classified programs was in the area of manufacturing and materials. One of the key challenges to the A-12 program was in the area of manufacturing. The structural members and the external skins used in the design of the A-12 included a high percentage of composite materials. Further, because of the nonconventional configuration, the size of many of these structural members and skins

was larger than had been produced by either GD or MCAIR. Any modern combat aircraft will have access panels and doors, mating surface discontinuities, mismatches at joints, and various other openings, which in turn cause cracks, gaps and other discontinuities to exist on the airplane's surface. From a [REDACTED] perspective (at the levels required of the A-12), these surface features posed a significant challenge to the Contractors because they had to make the airplane as continuous (smooth) as possible over the entire upper and lower surfaces -- more than 2600 square feet -- in order to achieve the RCS signature specification.

16. (U) Given the stage of development of the B-2 and F-117 programs, invaluable information from those programs on weight, LO suite development, and manufacturing/materials experience was available prior to the start of the A-12 Full Scale Engineering Development Program in January 1988. The lack of information from these other government-funded, classified, special access, LO aircraft programs adversely affected the A-12 Contractors' ability to predict accurately or achieve the government's requirements, and substantially increased the Contractors' development cost and schedule.

B. (U) McDonnell Douglas Experience at Time of Contract Award

17. [REDACTED] At the time of contract award, MCAIR had extensive experience in the design and development of sophisticated tactical aircraft, both carrier and land based. MCAIR also had experience in reducing the radar cross section (RCS) of existing aircraft designs. What MCAIR lacked was experience in bringing a [REDACTED] aircraft through full-scale development.

18. [REDACTED] In the ATA Request for Proposal (RFP) the Navy gave the Contractors the opportunity to submit additional classified information to enhance our credibility in the [REDACTED] arena. In January 1987, as part of the preparation of the MCAIR ATA proposal, S. A. LaFavor, Director of Advanced Development and Analysis at MCAIR, wrote to the Air Force Special Assistant for LO Technology, requesting permission from the Air Force to submit data from other MCAIR programs as part of a MCAIR addendum to the ATA proposal (Ex. A, 206//00577-87). MCAIR then submitted a classified, special access addendum to the proposal containing potentially relevant information from other compartmented programs to provide the Government with insight into the other programs involving low observables with which MCAIR had experience. This document was not submitted under the ATA codeword.

19. (U) At the time of the ATA proposal preparation, GD was considering Lockheed as a possible subcontractor to build parts of the wing trailing edge. Both GDFW and Lockheed also submitted separate codeword classified addenda directly to the government in March 1987, as specified by the RFP. These addenda were not permitted to be shared among the Contractors.

20. (U) The classified appendix submitted to the Court by the Government on May 27, 1993, included a redacted copy of the LaFavor letter and excerpts from the indices of the separate MDC, GD and Lockheed addenda. The first knowledge that I had that Lockheed had submitted F-117 information as part of its addendum was from the government's May 27, 1993 classified appendix. Access to the Lockheed-generated submissions, whatever they contained, was never given to me, or, to the best of my knowledge, to anyone at MCAIR

21. (U) Although I participated in early 1987 in requesting information from other MDC classified programs to be submitted in MCAIR's classified, special access addendum, I did not see nor was I made aware of the contents of the MCAIR addendum until after termination of the A-12 contract. I have subsequently reviewed the information contained in the MCAIR addendum and the LaFavor letter. The information contained

therein showed MCAIR involvement in several programs. I have further determined that the information presented was of little or no value to the A-12 detailed LO design and integration effort during FSED.

22. [REDACTED] The lack of helpful design information available within MDC at the time of the A-12 contract award is confirmed by a government document evaluating the relative capabilities and experience of various aerospace companies. In the 1984 time period, when contractors were being considered by the government for the ATA program (as the A-12 program was then known), neither GD nor MDC had served as principal designers of [REDACTED]low observable[3] aircraft. A government memorandum from approximately 1984, justifying the capabilities of various companies to participate in the Advanced Tactical Aircraft [REDACTED] concept

[3] [REDACTED] In the Navy community low overserable (LO) [REDACTED] defined as two different concepts. "LO" addresses the reduction in signature of an existing vehicle -- one which was not originally designed with signature as a requirement -- by application of spray-on radar absorbing material (RAM) to various components such as the wing. There are limits to the signature reduction which LO vehicles can achieve simply because of the pre-existing vehicle design features. [REDACTED] Typically [REDACTED] are [REDACTED] LO signature levels (radar detection range reductions of 50% or more). Additionally, because of the low radar cross section (RCS) levels, design details, such as how [REDACTED] panels are attached to [REDACTED].

formulation studies, rated the top four design leaders: Lockheed, Northrop, GD and MCAIR (Ex. B, 201//02285-90)[4].

23. [REDACTED] The justifications memorandum rated the four companies' experience in several areas: [REDACTED] developmental and flight experience. LO flight experience, [REDACTED] technology experience, tactical aircraft design and production, and carrier suitability. (See Ex. B, p. 1-2), The memorandum rated the design leaders by the amount of government investment in [REDACTED] technology, with Lockheed having received $10 billion, Northrop $5 billion, GD $2 billion, and McDonnell Douglas $10 million. The government thus had spent more than 1000 times more money with Lockheed, and over 500 times more with

[4] [REDACTED] This document was provided to plaintiffs through the discovery process in this case. Although the document bears a 1990 date, another document produced by the government suggests it was prepared in the fall of 1984. (See Ex. C). The latter document is the minutes of a September 26, 1984, meeting of the Special Program Review Group (or SPRG), a high-level Navy group which reviewed the Navy's classified special access programs. In discussing why only the four design leaders would be issued a Request for Proposal for the [REDACTED] program, Rear Admiral Santone stated that "if provided with sufficient information/justification regarding previous government (i.e., Air Force) investments, he could build sufficient rationale for exclusion." (Ex. C, OPNAV//0032-84, p. 2). Rear Admiral Sansone is a coauthor of the justifications memorandum. (Ex. B, p. 4).

Northrop, than it had with McDonnell Douglas.

24. [REDACTED] Additionally, the memorandum recognized Lockheed as being the national leader in applying [REDACTED] technology to flight aircraft, Northrop as being the most advanced [REDACTED] contractor, and both Lockheed and Northrop as having [REDACTED] flight experience.

25. [REDACTED] The memorandum described GD's experience as involving LO reduction on in-service aircraft and a unique aircraft design approach designed as a result of company-funded efforts. The memorandum stated that MDC had reduced the signatures of existing aircraft and was involved in [REDACTED] technology projects.[5] The memorandum noted that neither GD nor MDC had carried a [REDACTED] design to full scale development.[6]

[5] (U) One member of the SPRG explained at the September 1984 SPRG meeting that MCAIR was included on the list of principal design agents because of its "significant retrofit experience." (Ex. C, OPNAV/ /0032-84, p. 2).

[6] [REDACTED] The Navy's view of the experience of MCAIR and GD had not changed appreciably by mid-1986. An Executive Review briefing from late June 1986, after the two teams of contractors had completed the concept formulation phase, provides the following comparisons of the capabilities of the two teams:

26. [REDACTED] Developing a [REDACTED] design to full scale demonstration is precisely where the design and technology concepts are refined and integrated into a detailed design, resulting in a producible aircraft. This development knowledge existed at Northrop through its work on the B-2 and at Lockheed through its work on the F-117; it did not exist at MDC.

27. [REDACTED] Overview and conceptual information is of minimal use in developing the details which make a [REDACTED] design

> "o GD-MCAIR has tactical aircraft but questionable [REDACTED] technology and weight estimation
>
> o N-G-V [Northrop-Grumman-Vought] has [REDACTED] technology and design flexibility"

(Ex. 10 to Motion for Summary Judgment on Count IX, LIT/1985-93, p.27), and

> "o GD-MACAIR [sic] has a CV (carrier) based tactical aircraft but questionable [REDACTED] technology
>
> o Northrop-Grumman-LTV has [REDACTED] technology and a scaled down strategic bomber"

(*Id.*, p. 13)

Similarly, minutes of the ATA Source Selection Advisory Council from April 1987 states that the disparity between the GD-MCAIR (208) and Northrop (212) proposals "could indicate that because 212 has more experience in technology and manufacturing they are aware of the costs and have proposed a realistic figure while 208 has minimal experience and may not know what they're getting into." (Ex. 11 to Summary Judgment Motion on Count IX, p. 3)).

successful. The vital information necessary to implement a [REDACTED] configuration efficiently requires design data at the detailed level. Successful [REDACTED] design is not a conceptual design problem; it is dependent on implementation of details. For example, the knowledge that a particular [REDACTED] is composed of [REDACTED] is of minimal value. Howeve., the detailed information for this [REDACTED] installation is vital for use in the development of an aircraft such as the A-12. Such details as the external skin material and coatings, the adhesives used to attach the skin to the internal radar absorbing material, the materials and design of the internal radar absorbing material, and methods of attaching this material to the primary wing structure are all vital elements of [REDACTED] design. Incorrect design of any one of the above details can destroy the RCS reduction effectiveness of the [REDACTED]. To efficiently achieve a successful [REDACTED] design, MDC and GD required detailed access to designers, electronic (RCS) engineers, and data bases from other [REDACTED] programs to obtain the details.

28. [REDACTED] Further, the simple knowledge of the use of a given component on the B-2 is not enough; detailed knowledge of [REDACTED] integration of that component into the B-2 airframe is equally as critical. For

example, the knowledge that a particular radar antenna is used is of virtually no use without the details of how the antenna is installed in the aircraft to achieve a [REDACTED] design.

C. (U) Contractor Efforts to Obtain Information

29. [REDACTED] Beginning in the spring of 1986 and continuing periodically thereafter, I had several meetings at the Navy ATA Program office in Arlington, Virginia with Nat Haskell, the Navy's Deputy Program Manager for the ATA program, for the express purpose of requesting [REDACTED] information from the B-2 program. As Deputy Program Manager, Mr. Haskell handled all technical subjects for the Navy relevant to program management, including LO. At each meeting, I made Mr. Haskell aware of the Contractors' need to obtain the B-2 information in order to enable us to utilize existing technologies and to avoid duplicative development.

30. (U) Mr. Haskell responded to each of my requests for B-2 information by stating that the contractor team which won the ATA FSED contract would be granted access to the B-2 information. During this same time period, other Navy representatives, such as Terry

Cooney and Doug Greene, made statements to me consistent with Mr. Haskell's assurances.[7]

31. [REDACTED] During these conversations, all of the Navy representatives acknowledged the existence of the B-2 program and the identity of Northrop as the contractor. Without exception, the Navy representatives assured me that access to the B-2 information would be given as soon as the contract was awarded. The Contractors fully expected the Navy to honor this commitment. None of these Navy representatives ever stated that they would not be able to provide us with access to the B-2 information because it was classified, special access, or that we should stop requesting the information and would have to proceed with the [REDACTED] development of the A-12 in isolation.

32. (U) During this time period, GDFW made written requests to obtain the B-2 information for our joint use on the A-12 program. I participated in the development of the list of requests that GDFW provided to the Navy. On May 22, 1986, the Contractors requested

[7] (U) Indeed, the SPRG recognized in September 1984 that the A-12 program would draw on Air Force experience. Vice Admiral Busey stated at a SPRG meeting that the Navy acquisition strategy for the A-12 "would take full advantage of the substantial U.S. Air Force investment." (Ex. C, OPNAV//0032-84, p. 1).

information from the Navy regarding the following subjects:

Windshield, canopy metallized alloyed coating

LO door design, seals, fastening concept

Engine acoustic signature data

Inlet data: performance data on LO inlets

LO air data system

High-temperature, LO material information

Engine exhaust plume detection, infra-red signature information

Surface treatments

Secure flight test programs

Avionics/electronic warfare/LO information.

The Contractors also requested documents containing non-LO related information.

33. [REDACTED] In response to the Contractors' written request, the Navy provided the Contractors with a list of industry and government contacts who were working on various LO projects. However, the Navy did

not provide any additional assistance at the time. On MCAIR's behalf, I had my people contact the Navy's suggested sources, but the sources were not able to provide us with relevant information because need-to-know security restrictions from both the [REDACTED] program and the other programs we contacted were not removed by the Navy.

34. (U) From the commencement of the ATA (later, A-12) Dem/Val contract in early 1986 through FSED contract award in January 1988, I periodically reminded the Navy representatives that we still needed the B-2 information. Their responses consistently recognized our need for the information and stated that the information would be provided after contract award.

35. (U) Within a month after FSED contract award, I reminded Jeff Cook, who had taken over from Cdr. Terry Cooney as the ATA Class Desk Officer, of the Navy's commitment to provide us with access to the B-2 program if we were awarded the A-12 FSED contract. Capt. Cook acknowledged that the Contractors needed access, and that the Navy was "working on it." Subsequently, I raised the issue with Capt. Cook approximately every four to six weeks. Each time, his response was that the Navy was "working the problem."

36. (U) During FSED, as during the Dem/Val phase, the Contractors made written requests to obtain the B-2 information in addition to my verbal requests. At the Initial Design Review in April 1988, the Contractors submitted formal Requests for Reply ("R/R") to the Navy (R-SIG-009 and -010, attached as Exhibits D and E), seeking detailed design information on: (1) high temperature LO materials; (2) resistive sheet materials; (3) honeycomb cores; (4) electro-optical window coatings; (5) LO electronic surveillance measures antenna suppliers and experience; (6) LO canopy experience; and (7) LO seal, gap filler, and fastener information. The Navy never responded to the Contractors' Requests for Reply.

37. (U) On several occasions during FSED contract performance, the Navy referred to information in its possession of the type verbally promised by Navy representatives and formally requested by the Contractors. For example, in R/R R-SIG-004 (attached as Ex. F), the Navy criticized the Contractors' canopy coating technique, citing "maintainability and reliability problems" experienced on "previous programs." Similarly, R/R R-SIG-007 (attached as Ex. G) stated that "previous LO vehicles" had experienced problems with dangerous levels of static discharge from radar absorbing structure. In addition, at the IDR canopy

session the Navy commented on "better" LO seal designs than those presented by the Contractors. The Navy did not disclose any further details of its knowledge in any of the above areas to the Contractors.

38. (U) In August 1988, the Navy agreed to provide a briefing on the compartmented B-2 program for a very limited number of A-12 personnel. I was one of only two engineering directors from the Contractors to be cleared for the briefing, given on September 13, 1988. The briefing was a top-level overview provided by Air Force B-2 program personnel. (The other person briefed was Keith Jackson of GDFW.)

39. (U) About a month in advance of the briefing, Keith Jackson and I prepared and submitted to the Navy a list of specific information needed for A-12 development which we believed had been addressed on the B-2. However, the information actually provided at the 2-3 hour briefing was very limited and general in nature. There was very limited discussion of problems encountered, methodologies, materials or approaches.

40. (U) Within two weeks after this initial briefing, I again contacted Capt. Cook. I told him that we needed much more detail than we received at the September 13th B-2 briefing and repeated my request for a thorough, detailed briefing. I also provided Capt. Cook with another copy of the list of specific LO

information we needed, as well as a supplemental list. (An example of the information requested is attached as Ex. H). Capt. Cook again assured me that he would work on it.

41. (U) In May 1989, the Air Force sent an Independent Review Team ("IRT"), composed of Air Force personnel (several with B-2 experience), to assess the Contractors' A-12 LO design philosophy and progress. During Contractor briefings to the IRT, Air Force members of the IRT expressed their concerns with a number of the Contractors' designs. In addition, the IRT repeatedly made general references to information contained in other programs and to other contractors that could provide useful information concerning various LO problems. However, the Air Force never provided the Contractors with specific information of value or access to the other programs.

42. (U) In August 1989, I was one of approximately sixteen manager-level Contractor personnel to be briefed onto the Air Force's F-117 program. We were permitted to tour the Air Force base where the F-117 aircraft were located, inspect the aircraft, and speak with Air Force maintenance personnel. However, because neither Air Force technical representatives nor representatives of Lockheed, the F-117's prime contractor, were available, we were not able to obtain any

significant design details, or to determine the levels of radar cross section obtained on this aircraft. Subsequent requests for this data to the Air Force received no response.

43. (U) The first significant exchange of LO data between the A-12 and another classified, special access program (the B-2) occurred in January and February 1990. This data exchange in 1990 was made possible when several A-12 Contractors' personnel were cleared onto the B-2 program and several B-2 Contractors' personnel were cleared onto the A-12 program. Meetings were then held, at which detailed, classified special access LO data from both the A-12 and the B-2 were exchanged. Navy and Air Force representatives were present at these meetings.

44. (U) The information from the F-117 and B-2 briefings was either too general in nature or was received too late to be useful in the A-12 baseline design because, by February 1990 (the first significant exchange of detailed B-2 data), 90 percent of the A- 12 drawings had been released.

45. (U) During the A-12 FSED program, MDC utilized all known resources and information channels attempting to obtain the B-2/F-117 superior knowledge information that the Navy did not provide. These efforts did not yield helpful information.

46. (U) Other classified, special access required programs to which I had access from 1986 through 1990 did not contain the detailed LO design implementation data vital to the success of the A-12. If I had possessed knowledge of such data from another program we would have used it for preparing our bid and proposal and for A-12 development, after obtaining the appropriate clearances and authorizations from the government.

47. (U) Although security restrictions would have prevented my obtaining classified information from programs to which I did not have access, senior individuals at MCAIR who were aware of the A-12 program and other classified, special access MCAIR programs would have sought government approval for appropriate cross-clearances for A-12 engineers to MCAIR programs containing design implementation data helpful to the A-12, if such programs had existed.

48. (U) Moreover, I am aware that a number of classified documents which originated outside the A-12 program were transferred into the program and were reviewed by MDC A-12 LO engineers. In some cases, I directed that my A-12 engineers obtain and review data. In other cases, data was independently obtained and reviewed. The extent to which these documents contained information helpful to the A-12 effort is described in the Declaration

of Wayne C. Crouch, attached as Ex. 21 to Motion for Summary Judgment on Count IX.

49. (U) In my May 26, 1993 declaration, I discussed several documents produced by the government from its A-12 files which showed that the government had not met its obligation to provide vital information from other relevant programs (5-26-93 Farr declaration ¶¶ 19-21). Additional discovery from the government has yielded several more documents which show recognition by the government that it did not provide information from other programs to the A-12 program in a timely manner, if ever.

50. (U) For example, a June 20, 1989 memorandum to the Service Secretaries from the Office of the Undersecretary of Defense for Acquisition (Ex. I) endorses the idea of sharing technical information among participants in different stealth programs, discusses efforts to share F-117 experience with the A-12 program, and directs the Service Secretaries "to examine what additional initiatives should be undertaken involving other programs such as B-2 and LHX." A handwritten note on the memorandum states that the memorandum "was intended primarily to put pressure on Air Force staff and PMO to provide tech[nology] transfer. Navy (including prime contractors) access to F-117A and B-2 lessons learned (esp., manufac[turing], support, & maint[enance] previously initiated at staff level." It is clear

that the Navy was aware of their obligation to give the Contractors access to these other programs, and was further aware that they had not met their obligation.

51. (U) A mid-1990 memorandum from the files of the Program Analysis and Evaluation staff of the Office of the Secretary of Defense (Ex. J) confirms that no meaningful exchange of information from the B-2 program began until early 1990. The memorandum, which is organized chronologically, states that, in the period before FSED, "B-2 still classified, but some technology transfer expected." In the period from 1988 through early 1990, "[l]ittle if any data [was] provided on B-2 program," according to the memorandum. Only after early 1990, with the Critical Design Review in process, did "[i]nitial data exchange" with the B-2 program begin.

D. Weight

52. (U) The effect of weight on aircraft performance is significant; an increase in weight affects important performance items such as carrier takeoff and landing speeds (so-called wind-over-deck requirements), payload (how many pounds of weapons the airplane can carry), and range (how far the airplane can go from the carrier to a target). The Contractors' initial weight estimates were low due to the lack of relevant information --

namely, B-2 and F-117 weight experience -- in the Contractors' weight estimating data bases.

53. (U) This information, if provided, would have been incorporated into the Contractors' data bases and would have provided a more accurate weight estimation. Access to B-2 and F-117 weight data, including specifically weight histories, weight trade studies, structural weight growth, and LO suite weight growth, would have significantly aided the Contractors in dealing with the A-12's weight, cost and schedule increases, as described below.

54. (U) Following the Contractors' ATA proposal submittal in March 1987, the Navy provided an evaluation of the weight of the MCAIR/GD offering which indicated that the Navy-estimated weight was 2809 lbs heavier than the Contractors' estimate. Although some breakout of the Navy overweight estimate was provided, reasons or substantiation for the increased weight were not provided in many areas. The Navy would not elaborate on the background or other information which it had used to make its assessment. Where no Navy rationale or additional information was provided, the Contractors were constrained to simply reassess their assumptions and weights, since they had no technical basis for taking action to change the previous estimate. Substantiating information which the government knew to be more representative of

the ATA configuration was not provided. However, on those items where the Navy provided the rationale for increased weight of given components, the Contractors developed and incorporated revised increased weight estimates.

55. (U) As MCAIR and GDFW began detailed design and development of the A-12 airframe structure, we found that the resulting weights for the detailed designs of the structure were significantly in excess of the estimated weights which we had used in preparation of our BAFO. We initiated weight control and reduction measures which were unprecedented in the history of both MCAIR and GDFW. First, at MCAIR in mid-February 1988, I established a Weight Review Team consisting of a group of senior engineering experts in design, structure, and weights. The Weight Review Team reported directly to me. Their charter was to review all drawings for overweight parts, and to review parts which had an estimated weight of five pounds or greater. Secondly, the Weight Control Board, which was chaired by me, reviewed configuration items and potential changes which required management action to effect changes to bring the overall A-12 weight back to its target level. In addition, the Weight Control Board reviewed the monthly weight status reports prior to their submittal to the Navy. The third effort was the Weight

Reduction Committee, which reviewed inputs and suggestions solicited from all A-12 engineering to determine potential weight reductions and to assess possible specification deviations to achieve those reductions. This committee also reported to me. The Contractors' weight reduction emphasis was transmitted to our subcontractors, as well as to the NAVAIR engineers. This information was routinely shared with the Navy engineers to get them to renew their commitment to obtain the superior knowledge information needed by the Contractors to understand and correct this growth. Unfortunately they were unsuccessful in gaining timely access to this information.

56. (U) Approximately 50 percent of the A-12's overweight condition occurred in airframe structure weight and approximately 25 percent occurred in the LO suite.

57. (U) During the B-2 briefings which we received in early 1990, we were told that the B-2 had significant weight growth problems during development. My understanding from these briefings is that the B-2 weight growth likewise occurred in the airframe structure and the LO suite areas. We were told that the B-2 experienced weight growth well beyond estimates. In the B-2 briefing in early 1990, we were not given, nor have we ever received, details of the B-2 weight histories, weight trade studies, or corrective actions taken to

control B-2 airframe structure and LO suite weight growth.

58. (U) Had MCAIR and GDFW known and understood the details of the causes and areas of B-2 weight growth, our approach to the A-12 design development would have been substantially modified. For example, we would have estimated a heavier weight for the aircraft, and would have developed a structural certification plan based on this higher weight airframe; we would have increased the propulsion system thrust levels for carrier operations (for improved rate of climb if one engine fails during take off); we would have begun studies to evaluate flight control modifications very early in FSED to further reduce the A-12 approach speed to the carrier (for improved aircraft control, landing speed, etc.); and we would have made early, significant changes to the landing gear strength early to accommodate an increased A-12 aircraft weight (among other things, the gear acts as a shock absorber in carrier landings). If the B-2 and F-117 weight experience and schedule slippage information had been provided to MCAIR and GDFW, the amount of program risk in these areas would have been evident, and the weight and schedule areas would have been addressed with this knowledge from prior programs. Specifically, I would have recommended that the Contractors not commit to the weight level

guaranteed in the specification or to a 30-month schedule for first flight if the information on the B-2 weight and schedule history had been available.[8] Since the information was not made available, we entered into the FSED contract and proceeded with program performance on the mistaken assumptions that our proposed specification weight and development time span and cost were reasonable and achievable. After contract award, no information was provided by the government showing the unreasonableness of the A-12 cost and schedule compared to that of the B-2.

59. (U) The Contractors were forced to do weight estimation and weight reduction/control work without the benefit of government-funded B-2 knowledge to help focus our efforts more precisely in key areas, such as composite airframe structure and LO suite weights. Lacking this information, the Contractors experienced a cycle characterized by periods of rapid weight increase followed by time spans

[8] [REDACTED] Even with the knowledge it had obtained from the B-2, Northrop was only willing to propose a 36-month time span to first flight. In its August 1986 comments on the Navy's ATA Acquisition Strategy, Northrop explained that it did not endorse the 33-month schedule the Navy suggested, "primarily due to the increased design, tooling, manufacturing, and assembly time spans associated with a [REDACTED] vehicle system compared to those for a more conventional design." (See Ex. 25 to Plaintiffs' Motion for Summary Judgment on Count IX, p. 7).

of very little weight growth; and, at those times of relatively stable weight, the Contractors mistakenly believed that weight growth was under control. The Contractors' extensive efforts in weight control yielded results as the A-12 design moved toward completion. The A-12 projected overweight for the first flight aircraft remained constant for the last eight months of 1990. The A-12 weight growth was finally controlled, but only after tremendous expenditures of time and resources on the part of the Contractors. The Contractors projected a first flight weight for the aircraft of 5873 pounds in excess of the BAFO specification weight in December 1990.

60. (U) It is my understanding that the B-2 program was begun in 1981 -- approximately 7 years prior to the A-12 FSED start in January 1988. Information on B-2 weight, weight reduction efforts, weight penalties incurred so that other specification requirements could be met, and weight growth as a function of time would certainly have been available in January 1988 for our use.

61. (U) The F-117 LO suite weight, its weight problems and trade studies, and solutions developed for those problems were also available in January 1988. Materials, designs, manufacturing techniques, and technology advances were developed and available from both programs, which would have saved weight in the A-12 airframe structure and LO

suite, if the government had provided this information to us.

62. (U) In summary, the B-2 and F-117 weight experience in both the airframe structure and LO suite areas relating to weight estimation, weight control and reduction, and their impact on schedules would have provided vital information to the A-12 Contractors, which they would have used to make significant changes to the A-12 program.

E. (U) LO Information

63. [REDACTED] Low observability was a primary requirement for the development of the A-12. While the theory governing LO phenomena existed, the available analytical tools were, by themselves, not adequate to develop the designs necessary to meet the stringent Navy specification requirements. Thus, an empirical approach -- test, analyze and fix -- was necessary to develop the design to meet the A-12's [REDACTED] requirements. Without access to and use of specific technologies from other classified programs such as the B-2 and F-117, MCAIR and GDFW found that the effort required to design and integrate LO components into the A-12 airframe successfully consumed significantly more time and resources than we had anticipated. A very inefficient "test/analyze/redesign/retest" iterative procedure became necessary to achieve the RCS and IR levels required for the various systems, subsystems and components to reduce the overall aircraft RCS and IR signatures to the specification requirements. The final designs took more development time, were much heavier and more complex than expected, and significantly exceeded our expected schedule time spans and weight allocations.

64. (U) The Contractors conducted substantial exploratory research and development work at three major radar test facilities (Gray Butte

(California), RAMS (New Mexico), and Meridian (Texas)) as part of the effort to develop an RCS and IR compliant configuration for A-12. Unforeseen problems were encountered in, for example, the propulsion system and its components, including inlet and exhaust, antenna integration, electro-optical window integration, canopy integration, and control surface designs. The B-2 LO information and development experience in particular would have been of significant value in reducing our scope of work had we been given access to the data by the government.

65. (U) For example, LO data from the propulsion systems[9] of other LO aircraft was especially important to the A-12 design. The B-2 and the F-117 inlet designs incorporate features and design approaches that are significantly different from those developed for the A-12. Yet, the B-2 and the F-117 design data were directly relevant to the A-12 because all three are subsonic (as opposed to supersonic) aircraft which operate in the same flight regimes and would encounter the same threat environment. The unique features of their

9 (U) The propulsion system (or Integrated Engine/Exhaust System for the A-12) consists of three basic elements: an inlet (to let air in); an engine (to compress the air and mix the compressed air with fuel to be ignited to propel the aircraft forward); and an exhaust (to expel the hot gases from the engine [REDACTED].

inlet designs demonstrate that the B-2 and the F-117 programs developed data and design approaches, including successes and failures, which would have been extremely valuable and time-saving. The Contractors were forced to conduct an extensive research and development effort on the A-12; B-2 and F-117 information could have prevented the Contractors from engaging in efforts the government knew to be fruitless or wasteful. MCAIR and GDFW had no benefit of the government-owned results of trade studies, configuration development histories, and lessons learned and were forced to proceed with the A-12 propulsion system development in isolation. A commitment to provide this information was specified in the Navy's OR, and was relied on by the Contractors as part of the A-12 development BAFO.

66. (U) Substantial inlet design research and development effort was required to obtain the RCS levels necessary to meet the overall Navy RCS levels and other relevant requirements. In some cases RCS levels could not be achieved in spite of multiple redesign iterations. These difficulties were not anticipated by MCAIR and GDFW but were understood by both the B-2 and F-117 contractors because their design experience preceded that of the A-12 by several years.

67. (U) The exhaust nozzle design was perhaps the most difficult LO design challenge for the

A-12. Both the B-2 and the F-117 nozzle designs incorporated features which were relevant to the A-12 design in terms of both IR and RCS signatures. MCAIR and GDFW had no access to the design details, trade studies and test data for these programs, even after March 1990 when some details on the B-2 were revealed.

68. (U) Because of the complexity of the nozzle design, the interplay of several design characteristics was critical, including nozzle/exhaust IR signature, RCS signature, nozzle surface temperatures and cooling methods, nozzle performance, weight, and nozzle cooling air pumping capabilities. The problem is further complicated by the non-uniformity of the hot exhaust gases. "Hot streaks" in the exhaust caused localized temperature gradients on the nozzle surfaces which were unexpected and yielded an unsatisfactory design. These problems had been addressed on both the B-2 and F-117 nozzles; nevertheless, the information was not provided to MCAIR and GDFW by the government.

69. (U) In March 1990, a review of the B-2 inlet and nozzle revealed design information that would have had major impacts on the A- 12 design and test development planning, if the Contractors had been given access to this program. Details of this information are classified by the B-2 program.

70. (U) An additional critical design area for low observables is the aircraft air data system. The air data system acquires the pressure and temperature information needed to establish the aircraft altitude, speed, and angle of attack. The A-12 contractors, encouraged by the Navy, pursued two parallel approaches for low observable air data systems -- a laser-based system and a flush-mounted system. The Contractors spent millions of dollars and approximately a year of research and development on the laser-based system. Access to the B-2 design details in 1990 revealed that the B-2 employed a flush-mounted air data system which had been proven in flight test. During the FSED, the A-12 contractors had independently determined that the flush-mounted system was the preferred approach for the air data system, after unnecessarily expending enormous resources evaluating the laser-based system. We re-invented and developed a design concept for the A- 12 which had already been developed for the B-2 under government funding.

71. (U) Summarizing, LO information from the B-2 and the F-117 was vital to the successful execution of the A-12 FSED contract within the required cost and schedule. Government-owned information was available from these programs, both of which preceded the A-12 FSED by several years. Although the LO information which the Contractors needed

ranged from propulsion system design concepts to such details as design criteria for vents in the external surfaces, the technologies and techniques required by the Contractors were quite specific and focused. In order to achieve the A-12's stringent specification levels for RCS and IR (in combination with other Navy requirements such as Reliability and Maintainability, Interchangeability and Replaceability), the Contractors expected information from other government-funded classified LO programs to assist in achieving those stringent RCS and IR requirements within the program cost, weight, and schedule constraints. Contrary to the Contractors' expectations, no such information was provided in a timely manner; the Contractors, with the Navy's full knowledge, were forced to conduct an R&D project to develop those LO technologies for the A-12 at considerable expense in terms of cost and time.

F. (U) Manufacturing Information

72. (U) In order to achieve levels of surface fidelity required by the A-12's LO specification, the larger underlying structural assemblies also had to be made with the ultimate LO goal in mind. Manufacturing of both the B-2 and the F-117 had been in progress for years prior to the A-12 FSED. Review of the B-2 in March 1990 showed use of large composite structural members supporting a thick-wing design, very

similar to the design of the A-12. No detailed discussions were held on composite fabrication and assembly problems of large composites, or addressing design changes required to assembly tooling. During the course of the B-2 assembly line review, however, some unique tooling was noted, and some comments were made regarding difficulties of mating major composite subassemblies. Statements were also made regarding tooling changes necessary to accommodate difficulties encountered at the manufacturing splices.

73. (U) It is my understanding that the major assembly manufacturing areas for the B-2 are now unclassified. On information and belief, the initial B-2 manufacturing problems were extensive with numerous defects found in the initial composite part fabrications. Both Boeing and LTV (Northrop's major subcontractors on the B-2) encountered numerous composite manufacturing process problems and spent an extended amount of time resolving them. To my knowledge, the problems are essentially all resolved at this time. The benefits of the B-2 composite manufacturing experience would have been of significant value to MCAIR and GDFW in rapidly maturing our large composite fabrication processes and in correction and modification of processes to eliminate flaws and defects. The MCAIR and GDFW problems encountered in composite part development

were very similar to the experience as described above. None of this information was provided to us by the government.

74 (U) In the materials area, during our B-2 briefing in March of 1990, we found that a qualified graphite/epoxy composite material was available that had been developed for the B-2. In fact, the resin binder material that was developed was a better resin (in terms of its useable life) than that selected for A-12 use. This is particularly distressing because the supplier for B-2 composites and A-12 composites was the same company, which could not disclose its knowledge to the Contractors because of security restrictions imposed by the U.S. government.

75. (U) Other materials needed for the A-12 were previously qualified by the B-2 team but no knowledge of this information was provided to the A-12 contractors. Specifically we found that a bismaleimide ("BMI") resin composite material had been previously qualified for use on the B-2. (The use of bismaleimide resin composite material is necessary where environmental temperatures are higher than normal epoxy resin can withstand.) A different BMI resin material had been selected by the A-12 Contractors for use in similar environments. In late 1990 after indicating that the A-12 BMI material was not satisfactory, the Navy suggested that we contact Northrop and obtain the B-2 BMI

material for use on the A-12. The government provided no information prior to late 1990 on the existence of this qualified BMI resin material or its use on the B-2.

76. (U) Based on the relatively small amount of information provided to us on the manufacturing and process experiences and based on the existence of qualified materials available from the B-2 program, information on B-2 manufacturing experience, processes, inspection techniques and materials developed for B-2 use would have significantly enhanced the A-12 manufacturing/material development activities.

(U) I declare under penalty of perjury that the foregoing is true and correct.

Executed this 18th day of November, 1993, at St. Louis, Missouri.

/s/ Albert P. Farr III
Albert P. Farr III

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION AND GENERAL DYNAMICS CORPORATION

Plaintiffs,

v.

THE UNITED STATES,

Defendant.

No. 91-1204C
(Judge Hodges

DECLARATION OF S. KEITH JACKSON, JR.

1. My name is S. Keith Jackson, Jr. I am presently an employee of Lockheed Corporation. During the A-12 program, I was Deputy Program Director, Systems Engineering for plaintiff General Dynamics Corporation.

2. My professional field is Aerospace Engineering. I have a Ph.D. from the University of Colorado in Aerospace Engineering Sciences.

3. I became involved in the A-12 program at its inception in 1984. From February 1988 to March 1991, I was Deputy Program Director, Systems Engineering, in the A-12 program for plaintiff General Dynamics. In that capacity, I had responsibility in the A-12 Principal Program Office for a all engineering analysis, design, and testing for

the A-12 program. This involved coordinating the engineering efforts for General Dynamics and McDonnell Douglas Corporation and serving as a management interface point for engineering questions with government engineering organizations.

4. From the inception of the A-12 program in 1984, I was aware generally that the government was conducting other stealth or low observable ("LO") weapon system development programs. For example, I knew from publicly available sources that the government had undertaken a development program for an advanced strategic bomber, later identified as the B-2, and that other government classified stealth projects were underway.

Requests for Information From Other Classified Programs

5. On several occasions during the Concept Formulation and Demonstration/Validation phases of the A-12 program (1984-1987), I attended meetings with various Navy and Air Force technical representatives at which I sought the transfer of information relating to advanced LO technologies from other government programs. In each instance, the information requested was not otherwise available to the A-12 contractors due to security restrictions imposed by the government. During these meetings, I emphasized the importance of obtaining this information in order to utilize existing technologies sponsored by the government, avoid duplicative development, and more accurately focus on technical hurdles in the design process. Because I was not aware of the details of the B-2 or other

government programs into which I had not been granted access, I was not in a position to request all of the specific information which I later learned would be critical in the development of the A-12.

6. At none of these meetings, or at any other time, did any Navy or Air Force representative express any unwillingness to seek the transfer of needed classified information into the A-12 program. To the contrary, Navy technical representatives appeared to understand the relevance of the requested information to the A-12 program, felt that the transfer of the requested information was desirable, and implied that technically beneficial information existed. These representatives committed themselves, insofar as existing security constraints permitted them even to discuss it with us, to actions that should have resulted in their providing the requested information. The government's response to our specific requests was consistent with the government's formally stated policy of sharing relevant information among its advanced development programs to prevent unnecessary duplication and redevelopment of technologies.

7. Because of our perceived need to improve the radar signature aspects of our design, during this time period General Dynamics made written requests to obtain B-2 classified information for our use on the A-12 program. In May 1986, we requested information from the Navy regarding the following subjects:

- Windshield, canopy metallized alloyed coating

- LO door design, seals, fastening concept
- Engine acoustic signature data
- LO inlet performance data
- LO air data system
- High temperature LO material
- Engine exhaust plume detection, infrared signature
- Surface treatments
- Secure flight test programs
- Avionics/electronic warfare/LO

We also requested many other documents containing non-LO related information on missile systems, ground systems, aerodynamic systems, electronic systems and technology, and other military systems.

8. In response to our written request, the Navy provided us with a list of industry and government contacts from other programs working on various LO topics. However, the Navy did not provide any additional assistance at the time. I directed our engineers to make appropriate contacts in accordance with the Navy's suggested sources, but the sources were largely unable to provide us with relevant information. Since this information was not provided, we were unable to learn what key lessons had been learned on other programs and how they might be applied to the A-12 design and development effort.

9. From early 1986 through the award of the Full Scale Engineering Development ("FSED") contract in January 1988, I periodically reminded Navy representatives that we continued to need relevant information from the B-2 and other classified programs. Their responses recognized consistently our need for the information and the desirability for us to have the information. These representatives promised that they would make every effort to provide the information after contract award and were optimistic that such exchange would be possible despite the government's stringent security constraints.

10. On several occasions after award of the A-12 FSED contract in January 1988, I discussed with Navy representatives our ongoing need for information from other government classified programs. At no time did any government representative refuse to seek to provide the needed information. Rather, in all cases the government representatives acknowledged the existence and relevance of the information, and agreed to assist us to obtain it.

11. During FSED, as during the Dem/Val phase, the A-12 contractors made written requests to obtain the B-2 and other relevant information. At the Initial Design Review in April 1988, the Contractors submitted Requests for Reply to the Navy seeking detailed design information on: (1) high temperature LO materials; (2) resistive sheet materials; (3) honeycomb cores; (4) electro-optical window coatings; (5) LO electronic surveillance

measures antenna suppliers and experience; (6) LO canopy experience; and (7) LO seals, gap fillers, and fasteners. The Navy never responded to these written requests.

12. The ATA Acquisition Strategy directed that the A-12 program take advantage of technologies being developed by the Air Force. To this end, the Air Force stationed an Air Force officer in the Navy's A-12 Program Office to assist with the program. This arrangement should have facilitated cross-service transmittal of information between Air Force programs (e.g., the B-2 and F-117A) and the A-12 program.

13. Not until August 1988 did the Navy and Air Force agree to provide the A-12 contractors with a substantive briefing on compartmented B-2 information, and then only for a limited number of A-12 personnel. Only the contractors' two engineering directors (myself and Albert P. Farr from MDC) were cleared for the September 13, 1988 briefing by Air Force B-2 personnel. Although the Air Force briefers were responsive, the information actually provided at the 2-3 hour briefing was limited and general in nature. There was only limited discussion of the details of problems encountered, design and analysis methodologies, or materials approaches and performance. Security constraints (namely, the lack of cross-access by other A-12 cleared personnel) made it impossible to transmit any useful information that was obtained at the briefing to the A-12 contractors' working-level engineers, where it was most needed.

14. In May 1989, an Independent Review Team composed of Air Force personnel, many with B-2 experience, assessed the contractors' A-12 LO design philosophy and progress. The Air Force Team made repeated general allusions to information contained in other programs and to other contractors that could provide useful information concerning various LO problems. However, the Air Force did not at the time provide the contractors with specific information or access to other programs.

15. In August 1989, I was one of approximately sixteen manager-level contractor personnel to be briefed onto the Air Force's F-117A program. We were permitted to tour the Air Force base where the F-117A aircraft were located, examine the aircraft, and speak with Air Force maintenance personnel. Although the visit was useful with respect to operational and maintenance issues, due to the fact that no representatives of Lockheed Corporation were available (the F-117A prime contractor) and the lateness of the visit (more than one and a half years after FSED contact award), we were able to obtain little or no information useful to the A-12 design.

16. The first truly significant exchange of LO data between the A-12 and another compartmented program occurred in February 1990 when the A-12 contractors exchanged information with the B-2 program. However, this exchange of data was too late to be of value to the A-12 baseline design since approximately 90 percent of the A-12 engineering drawings had been released by that time. In furtherance of this exchange, working level meetings

between A-12 and B-2 personnel were on the verge of becoming broadly productive when the A-12 program was terminated in January 1991.

17. Based on information provided at the B-2 meeting in February 1990, it was evident that prior to 1986 much of the B-2 LO and other data were available and that significant design and development test work had been conducted. A knowledge of even generic and unclassified items such as the lengthy development history of the B-2 and of the weight growth for that aircraft would have been particularly valuable had it been made available to us before or during the A-12 FSED proposal development phase.

18. During the A-12 FSED phase, General Dynamics used all known resources and information channels attempting to obtain the B-2 and F-117A information that the Navy did not provide. These efforts did not yield helpful information to the best of my knowledge.

19. I am also aware that a number of the classified documents which originated outside the A-12 program were transferred into the program and reviewed by General Dynamics engineers. Information from these documents provided a modest benefit to the A-12 effort, but did not provide the type or quality of information that timely access to the B-2 and F-117A programs would have added to the contractors' A-12 design and manufacturing effort.

Decision Not to Enter In a Subpoena With Lockheed

20. During the Demonstration/Validation phase of the A-12 program, Lockheed Corporation provided the contractors with technical design assistance, surrogate LO materials, and a few selected other items of LO technology, primarily in support of full-scale RCS model tests. One of these items was an air data probe design which the contractors later learned was used on the F-117A. However, Lockheed's air data probe proved to be of no use to the A-12 design because of an incompatibility with A-12 radar cross section requirements. Due to government security restrictions, information from the F-117A program that might have proved useful in terms of aircraft design could not be shared with the A-12 contractors.

21. At the time of the best and final offer, we intended to enter into a subcontract with Lockheed to include work in the area of low observables, specifically optical air data systems, air data probes, and materials and structures work. However, a number of factors caused the contractors to abandon this effort.

22. First, Lockheed refused to accept many of the significant A-12 contractual requirements that were imposed by the Navy, including the LO specification requirements. Next, Lockheed's proposed prices for participation in the A-12 program were not competitive. Finally, in return for their involvement with the contractors on the A-12, Lockheed demanded, in addition to air data systems

work, a high minimum of guaranteed subcontract work.

Other GD Classified Programs

23. In the contractors' proposal, the contractors identified several other special access programs that we believed would be beneficial to the design of the A-12, particularly with regard to LO technologies. Each contractor, and Lockheed (see above), submitted appendices under separate code words to the LO volume of the proposal, describing other classified programs in which each company had been involved. Due to government security restrictions, the individual companies were unaware of the information contained in the other companies' appendices.

24. Other classified programs in which General Dynamics had been involved were listed in Appendix A to Volume 22F of the contractors' proposal. Only a very few people at General Dynamics were aware of the contents of this appendix. Information from the programs in which General Dynamics was involved proved of only limited use in the design of A-12 during FSED. The main value of such programs was the fact that some people who had worked on them were later assigned to the A-12 and brought generic knowledge form their earlier work along with them. Separate security compartments often prevented direct use of data from these other programs. A major shortcoming of the available database within General Dynamics was that it contained little or no information from other comparable aircraft programs, particularly the B-2

Declaration of Albert P. Farr, III

25. I have reviewed the November 18, 1993, declaration of Albert P. Farr III on this subject and find it accurate to the best of my knowledge. I concur with his statements regarding the contractors' need for superior knowledge in three areas – weight, low observables and manufacturing – in the design and manufacture of the A-12.

I declare under penalty of perjury that the foregoing statements are true and correct.

11/19/93	/s/ S. Keith Jackson, Jr
Date	S. Keith Jackson, Jr.

No. 91-1204C
(Judge Hodges)

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,

Plaintiffs,

v.

THE UNITED STATES,

Defendant.

DEFENDANT'S BRIEF IN SUPPORT OF ITS MOTION TO DISMISS PLAINTIFS' "SUPERIOR KNOWLEDGE" CLAIMS, AND RESPONSE TO THE COURT'S ORDER DATED NOVEMBER 1, 1993

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IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DEFENDANT'S BRIEF IN SUPPORT OF ITS MOTION TO DISMISS PLAINTIFS' "SUPERIOR KNOWLEDGE" CLAIMS, AND RESPONSE TO THE COURT'S ORDER DATED NOVEMBER 1, 1993

Plaintiffs possess the burden of proof to establish a breach of the implied contractual duty to share "superior knowledge." Plaintiffs have not made, and cannot make, a *prima facie* showing in support of this claim, and the Government cannot demonstrate the existence of possible defenses to that claim, because those matters are inextricably intertwined with military state secrets. Accordingly, plaintiffs' claim cannot be litigated and must be dismissed.

The military state secrets privilege may not be inadvertently waived, and the manner in which the Executive controls or manages access to classified information is not subject to review by the judiciary. There is, therefore, no reason for this Court to enter "findings" regarding that control of access. Rather, the Court is now called upon to resolve the purely legal question regarding the effect of the non-justiciability of plaintiffs' superior knowledge claims -- it is absolutely clear that, as a matter of law, those claims should be dismissed.

BACKGROUND

As a matter of background information, we are constrained briefly to clarify a few matters contained in the Court's November 1, 1993 recitation of the procedural history of plaintiffs' attempts to secure discovery of military state secrets in this case. [1]

I. Nature of the Dispute

Plaintiffs allege that the Government had, and breached, an implied contractual duty to share classified military secrets contained in "special access" programs, other than the A-12 Program at

[1]The Government is concurrently filing a classified, *ex parte* declaration and supplement to our brief, in order to specifically set forth factual details involving the Government's invocation of the state secrets privilege, and related matters. To clarify matters addressed in the Court's order dated November 1, 1993, it is necessary for the Court to review factual matters that can be presented only in this fashion. We incorporate that classified filing in this brief, by reference.

issue in this case.[2] Since such a duty cannot be implied because it would eliminate the Executive' s exclusive constitutional responsibility to control military secrets, the Government moved to dismiss plaintiffs' claims. The Court denied our motion to dismiss. The parties and the Court then began to struggle with difficult discovery issues. Unavoidably, plaintiffs' attempted discovery soon conflicted with the Executive's responsibilities to safeguard and manage military secrets.

The information required for litigation of plaintiffs' claims is contained in an indeterminate number of special access programs, including currently "unacknowledged" programs.[3] The Air Force initially allowed limited access for plaintiffs' attorneys to two programs (B-2 and F-117A).

[2] "Special access" represents a more restrictive classification of national security information than secret or top secret classifications. One may not convey "special access" information to another individual not specifically authorized to receive that information. *See* Executive Order 12,356 sec. 4.2 (April 2, 1982); 3/30/93 Donley Decl. ¶¶ 7-11.

[3] An "unacknowledged," or covert, program is a program the very existence of which is classified within the boundaries of the special access program. In other words, one must be approved for access before one can know that the program exists at all. *See* 3/30/93 Donley Decl. ¶ 10. Accordingly, information contained in an unacknowledged special access program cannot be shared in any way with individuals who have not been granted access, and it is not possible to "explain the situation," 11/1/93 Order at 6, regarding an unacknowledged special access program to one who is not cleared for access, without violating security restrictions. *See In re United States*, Misc. No. 374 (Fed. Cir., April 30, 1993), slip op. at 12.

Subsequently, however, the Acting Secretary of the Air Force formally invoked the state secrets privilege recognized in *United States v. Reynolds*, 345 U.S. 1 (1953), in response to an order directing disclosure of certain other information. This Court: (1) ordered expanded access to the B-2 and F-117A programs; and (2) ordered disclosure of additional privileged information. The court of appeals issued two writs of mandamus, directing that both of the non-A-12, "other-program" discovery orders be vacated.

In its most recent order on this subject, the Court correctly notes that extraordinary security measures are in place in this lawsuit. 11/1/93 Order at 2-3. Those measures are irrelevant, however, to the problems posed by plaintiffs' "superior knowledge" claims. At issue here is special access required information from other programs, including unacknowledged programs. No matter what measures are taken, what level of security clearances plaintiffs' lawyers possess, or to which programs the attorneys have previously been admitted, "this cannot mean that they are also granted access to *other* special access programs." *In re United States*, Misc. No. 374 (Fed. Cir., April 30, 1993), slip op. at 13 (emphasis in original). Indeed, as the Court notes at pages 8-11 of its recent order, the Executive's exercise of predictive judgment regarding military secrets in this case precludes litigation of plaintiffs' superior knowledge claims, notwithstanding security procedures that the Court might deem sufficient.

The Court's recent order also suggests that *Molerio v. Federal Bureau of Investigation*, 749 F.2d

815, 825 (D.C. Cir. 1984), and *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 547 (2d Cir. 1991), require more definite, or comprehensive, showings in order to necessitate dismissal of plaintiffs' claims. 11/1/93 Order at' 8. That is not the case. *See* Part 3.C., below. In any event, as we have previously demonstrated at some length, the privileged information in this case *does* represent a defense for the Government to plaintiffs' superior knowledge claims, as in *Molerio*. *See* Classified, *Ex Parte* Appendix, dated June 11, 1993. Consideration of the privileged information, in conjunction with an assessment of *all* of the elements of a superior knowledge claim, reveals that plaintiffs cannot establish such a claim. At the very least, development of the Government's factual defense would be "so hampered" as to require dismissal. *Zuckerbraun v. General Dynamics Corp.*, 935 F. 2d at 547, *citing Molerio v. Federal Bureau of Investigation*, 749 F. 2d at 825. In addition, there is no justification or reason for a further "comprehensive determination of information subject to the state secrets privilege." 11/1/93 Order at 8. Taken together, the formal invocation of the state secrets privilege in this case and the declarations of Acting Secretaries Donley and General McPeak more than establish that the "very subject matter of (these claims) is thus a state secret." *Zuckerbraun*, 935 F.2d at 548. Nothing more comprehensive was supplied, or required, for dismissal in *Zuckerbraun*.

II. The Parties' Actions In Connection With Plaintiffs' Attempts To Secure Superior Knowledge Discovery

As is necessarily established more fully in the classified, *ex parte* materials that we are submitting with this brief: (1) there was absolutely nothing improper about the manner in which program accesses for plaintiffs' attorneys have been handled in this case; (2) the security problems that arose in pre-trial depositions arose primarily out of the very nature of plaintiffs' claims, and the concerted and deliberate efforts of plaintiffs' attorneys to pursue those claims, rather than from any "security lapses" by the Government; and (3) there is nothing unique or improper regarding the access that attorneys for the United States have had to classified information in this case.

During the course of this litigation, the Air Force has protected from disclosure certain unacknowledged matters, and, accordingly, has formally asserted the military state secrets privilege. *See* 3/30/93 Donley Declaration. All of the protected information is under the control of the Air Force, and the Air Force has had to intercede to protect the security of those military secrets several times during the course of this litigation.

1. **Access of Plaintiffs' Counsel.** In August 1992, a representative of General Dynamics approached an Air Force officer and suggested that plaintiffs would seek access for their counsel to certain unacknowledged Air Force matters. In November 1992, General Dynamics submitted to the

Government a request for access for two of its attorneys to certain unacknowledged Air Force activities. The request for access itself was classified as "special access required." *See* Executive Order 12,356 sec. 4.2. The Air Force delayed consideration of this question between November 1992 and February 1993, in part because the question of what role, if any, the information might play in the litigation was not clear, and the parties and the Court were generally addressing "superior knowledge" discovery throughout that time period.[4]

[4] Specifically, various portions of the case were stayed, and the parties filed briefs concerning "superior knowledge" discovery on July 24, 1992; July 28, 1992; August 6, 1992; September 9, 1992; September 16, 1992; and September 29, 1992. Several times during this period, the Court met with the parties, and eventually a negotiated set of discovery requests, **limited to the B-2 and F-117A programs**, was served by plaintiffs on October 21, 1992. On October 30, 1992, the Court entered an order requiring responses to a limited number of interrogatories, and addressing the B-2 and F-117A discovery. On November 13, 1992, plaintiffs sought expedited discovery, again limited to the B-2 and F-117A programs. On November 22, 1992, Secretary Rice allowed limited access to the B-2 and F-117 programs for purposes of this litigation. By order dated December 2, 1992, the Court noted that "plaintiffs have agreed to the (discovery) conditions thus far." Discovery then proceeded within the B-2 and F-117A programs until February 12, 1993, when plaintiffs filed their motion for the expanded B-2 and F-117A access that eventually led to the issuance of a writ of mandamus by the court of appeals. *In re United States*, Misc. No. 370 (Fed. Cir., April 16, 1993). *See* 3/15/93 Plaintiffs/Respondents Opposition to Petition for Writ of Mandamus, Misc. No. 370, at 3 (requested discovery "limited to the B-2 and F-117A programs."). In sum, prior to February 1993, the Government, plaintiffs, and the Court were focused only upon the B-2 and F-

In February 1993, plaintiffs' counsel informally raised the issue with the Court. At or about that time, the Air Force reviewed the matter, concluded that access was not appropriate, and denied plaintiffs' request. The Court then ordered a briefing to plaintiffs' lawyers, which commenced the events that led to the issuance of a writ of mandamus by the court of appeals on April 30, 1993. *In re United States*, Misc. No. 374 (Fed. Cir., April 30, 1993), slip op. at 3-8.

2. Deposition Issues. Plaintiffs's pursuit of their "superior knowledge" claims resulted in serious security problems with respect to two pre-trial depositions: the deposition of Richard Rumpf on March 11-12, 1993, and of Admiral David Jeremiah on July 19, 1993.

At the deposition of Richard Rumpf, counsel for both plaintiffs posed a variety of questions that elicited responses implicating classified, special access information that has been excluded from the case pursuant to the Government's claim of privilege. Government counsel asked a very limited number of similar, follow-up questions at the deposition -- questions that never would have been asked, but for plaintiffs' inquiry.[5] At a subsequent hearing on

117A programs in connection with "superior knowledge" issues in this case, and not upon any other matters.

[5] As the court of appeals has explicitly held, such simple follow-up questions by Government counsel did *not* constitute an attempt by the Government to improperly "use" classified information to further the Government's case on the merits. *In re United States*, Misc. No. 374 (Fed. Cir. April 30, 1993), slip op. at 16, n.5.

March 23, 1993, plaintiffs' counsel read portions of the Rumpf deposition transcript into the record. Because the deposition excerpts constituted security violations, the Air Force took control of and redacted portions of the hearing and deposition transcripts. *See* Air Force letters to Messrs. Gaffney, Fenster and Ms. Mitchelson, dated April 22, 1993, App. 1-3. The bulk of the redacted material consisted of testimony given at the instance of plaintiffs, and not the Government. Moreover, plaintiffs' counsel received the redacted versions prior to surrendering the unredacted versions, and intentionally and deliberately created a document *highlighting* the redacted portions (thereby isolating and calling attention to the sensitive information). Counsel then attempted to file those highlighted versions of the transcripts with this Court and the court of appeals. with the approval of both courts, the Air Force also took control of those highlighted transcripts. *See*, Air Force letter to Court Security Officer, dated April 23, 1993, App. 4; CAFC letter to Air Force, dated April 26, 1993, App. 6; 4/27/93 Order, App. 7.

Subsequently, the court of appeals ruled that the Government's claim of the military state secrets privilege in this case must be sustained. *In re United States*, Misc. No. 374 (Fed. Cir. April 30, 1993). Despite the decisions by the court of appeals and the prior circumstances surrounding the Rumpf deposition, plaintiffs' counsel again probed the same sensitive area during the July 19, 1993 deposition of Admiral Jeremiah -- during a brief period when the Navy security officer was absent from the deposition session. Again, the Air Force was required to take

control of portions of the transcript resulting from the questioning by plaintiffs' lawyers, and redact the sensitive testimony. *See* Air Force letters to Messrs. Churchill and Gaffney, dated August 5, 1993. App. 8-9.

Finally, this Court stayed all superior knowledge discovery on August 11, 1993. *See* 8/11/93 Order. Nevertheless, in the subsequent deposition of captain Elberfeld, plaintiffs' attorneys *again*, over the protestations of the Government, deliberately and affirmatively sought to probe the same sorts of sensitive areas in connection with "superior knowledge" issues. *E.g.*, App. 10-12.

In sum, the history of the security problems arising from discovery in this action overwhelmingly demonstrates the non-justiciability of plaintiffs' "superior knowledge" claims, and that these issues uniformly arose from plaintiffs' concerted efforts to pursue those "superior knowledge" claims. The fact that those claims are non-justiciable is not in any way attributable to "security lapses" by the Government.

3. Access Of Government Counsel. In this case, as in every "state secrets" case that has ever been litigated, Government lawyers are aware, and necessarily must be made aware, of classified information that the private litigants' lawyers cannot know. There is nothing improper, unusual or inappropriate about the Government lawyers' access to classified information in this case.

Moreover, the Government has not been allowed to "use" the information for tactical purposes

in this litigation. *See In re United States*, Misc. No. 374 (Fed. Cir. April 30, 1993), slip op. at 16 n. 5. Because we believe the privileged information would be fatal to plaintiffs' claims on the merits, we certainly would have desired to make extensive use of the privileged information if it could be disclosed. Indeed, it is manifestly apparent that the privileged information is central to the resolution of any "superior knowledge" claim. The decision regarding disclosure, however, rested with the Air Force, which determined to assert the military state secrets privilege regardless of whether the information would support or hinder the Government. Since that time, we have not attempted to make tactical "use," or any "use," of the information -- it has simply been removed from the case. We do, however, recognize the conclusive and binding authorities that require dismissal in these circumstances, and recognize our duty to seek to secure such a dismissal.[6]

[6] There are other aspects of the Court's November 1, 1993 order with which we disagree. For example, pursuant to Secretary Rice's determinations regarding the B-2 and F-117A programs, it is not the case that "an infinite number of persons" could review the special access information in those programs, ten persons at a time. 11/1/93 Order at 10. Applicable program guides prohibit such intentional rotation of personnel, but the Air Force was willing to afford limited latitude on one specific occasion, because it accepted plaintiffs' representations that they did not initially foresee the substitutions that they later sought. In any event, those matters have been resolved. *In re United States*, Misc. No. 370 (Fed. Cir., April 19, 1993). Because, as we noted above, factual findings regarding the Government's control of access to classified information are not necessary or appropriate, we do not address other inaccuracies

ARGUMENT

In its order dated November 1, 1993, the Court directed the parties to address three issues:

> 1. Whether we should remove counts VI through XI from the case to the extent that they rely on the allegation that defendant breached its duty under the superior knowledge doctrine;
>
> 2. Whether we should make findings regarding the manner in which defendant controlled access to classified information prior to invocation of the state secrets privilege by Acting Secretary Donley; and
>
> 3. Whether we should enter judgment for plaintiffs if defendant's invocation of the state secrets privilege precludes them from litigating their superior knowledge claims.

11/1/93 Order at 12-13. We address each of these issues, in turn.

in the Court's recitation contained in its November 1, 1993 order.

1. **"Whether The Court Should Remove Counts VI Through XI From The Case To The Extent That They Rely On The Allegation That Defendant Breached Its Duty Under The Superior Knowledge Doctrine"**

All of the "superior knowledge" claims in the various counts of plaintiffs' complaint are based upon the Government's asserted failure generally to fulfill an alleged implied duty to share classified, special access information. For reasons discussed more fully in our response to the Court's third issue below, all of those claims must be dismissed.

As we previously demonstrated in our May 27, 1993 motion to dismiss, and as the Court has correctly held, *e.g.* 11/1/93 Opinion at 11, plaintiffs' general allegation that the Government possessed a duty to share some unspecified, classified special access information cannot be litigated in this case, because those claims are inextricably intertwined with military state secrets. Plaintiffs' claims are primarily contained in Count IX of their second amended unclassified complaint, and in their factual recitations at paragraphs 46-61. Those general allegations are repeated, however, in the context of other counts, as follows: Count VI (impossibility of performance), ¶¶ 234-235; Count VII (commercial impracticability), ¶¶ 250-251; Count VIII (mutual mistake of fact), ¶ 259; Count X (failure to cooperate/constructive changes), ¶ 281; and Count XI

(breach of implied covenant of good faith and fair dealing), ¶ 285.[7]

Plaintiffs' superior knowledge claims, whether averred explicitly in Count IX or obliquely in Counts VI through XI, cannot be litigated because those claims are inextricably intertwined with state secrets. Like Count IX, then, the other "superior knowledge" references in plaintiffs' complaint vaguely assert that some unspecified, unnamed classified special access information was not shared. Like Count IX, those claims "are inextricably intertwined with privileged matters." *Guong v. United States*, 860 F. 2d 1063, 1066 (Fed. Cir. 1988), (*quoting Fitzgerald v. Penthouse International. Ltd.*, 776 F.2d at 1243 n. 11), *cert. denied*, 490 U.S. 1023 (1989); *Bareford v. General Dynamics Corp.*, 973 F. 2d 1138 (5th Cir. 1992), *cert. denied*, 113 S. Ct. 1843 (1993). Like Count IX, those claims must be dismissed.

[7] In paragraphs 60 and 122-127 of their complaint, plaintiffs suggest that the Government breached an implied duty to share "superior knowledge" regarding which radar subcontractor plaintiffs should have retained. Plaintiffs' allegations are factually and legally deficient for a variety of reasons, but, to date, do not appear to turn upon, or to be inextricably intertwined with, matters subject to the absolute military state secrets privilege.

2. Whether The Court Should Make Findings Regarding The Manner In Which Defendant Controlled Access To Classified Information Prior To Invocation Of The State Secrets Privilege By Acting Secretary Donley"

The two decisions by the court of appeals in this case establish that this Court lacks jurisdiction to review the Executive's judgment regarding management of military state secrets. *E.g.*, *In re United States*, Misc. No. 374 (Fed. Cir., April 30, 1993), slip op. at 22 (citation omitted); *In re United States*, Misc. No. 370 (April 16, 1993), slip op. at 5, 15. The military state secrets privilege cannot be inadvertently waived, and the Government cannot be estopped from asserting the privilege in one set of circumstances, even where it has affirmatively chosen not to assert the privilege in another. *E.g.*, *In re United States*, Misc. No. 374 (Fed. Cir., April 30, 1993), slip op. at 14, *citing Northrop Corp. v. McDonnell Douglas Corp.*, 751 F.2d 395, 402-03 n.9 (D.C. Cir. 1984).

Accordingly, any additional "findings" regarding the Executive's control of access to classified information in this case would be legally irrelevant, and would go far beyond the issues that this Court is now called upon to resolve. Moreover, as demonstrated by the factual discussion above and by the additional *in camera* materials filed concurrently with this brief, there is no evidence whatsoever that any Government official has acted improperly in any way. Even if the case were in a procedural posture for the Court to hold otherwise,

there is not a scintilla of evidence, much less the "well-nigh irrefragable" proof necessary, to support such a "finding." *E.g., Kalvar Corp. v. United States*, 211 Ct. Cl. 192, 198 (1976). *See also, Spezzaferro v. F.A.A.*, 807 F.2d 169, 173 (Fed. Cir. 1986); *Sanders v. United States Postal Service*, 801 F.2d 1328, 1331 (Fed. Cir. 1986); *Gonzales v. Defense Logistics Agency*, 772 F.2d 887, 889 (Fed. Cir. 1985); *Hayes v. Department of the Navy*, 727 F.2d 1535, 1537 (Fed. Cir. 1984).

3. Whether The Court Should Enter Judgment For Plaintiffs If Defendant's Invocation Of The State Secrets Privilege Precludes Them From Litigating Their Superior Knowledge Claims"

Plaintiffs have asserted a non-justiciable claim that is inextricably intertwined with the absolute military state secrets privilege. It is well settled that a court must dismiss a non-justiciable claim, and not award judgment in favor of plaintiffs for their ingenuity in devising such a claim.

Plaintiffs' "superior knowledge" claims must be dismissed because: (a) plaintiffs' claims are, on their face, legally deficient because no duty to share this information may be imposed upon the Government; (b) plaintiffs' have not, and cannot, establish a *prima facie* case without privileged information; (c) the very fact that plaintiffs' claims are "inextricably intertwined" with state secrets requires dismissal; (d) plaintiffs possess, and cannot carry, the burden of establishing a "superior knowledge" claim; and (e) the rule requiring

dismissal in these circumstances is right, equitable, and appropriate.

A. A. Plaintiffs' Claims Are Legally Deficient

Application of the "superior knowledge" doctrine in the context urged by plaintiffs would violate the Executive's exclusive constitutional responsibility to exercise its judgment and expertise, in determining with whom "special access" military secrets will be shared. *E.g.*, *Department of Navy v. Egan*, 484 U.S. 518 (1988); Executive Order 12,356 sec. 4.2 (April 2, 1982),3 C.F.R. 166, 174 (1983). Therefore, plaintiffs' claims are deficient as a matter of law, and should be dismissed.

The United States Court of Appeals for the Federal Circuit, in the two mandamus opinions issued in this case, broadly, explicitly and unequivocally rejected the notion that courts may directly impose a duty upon the Government to disclose classified, special access information to plaintiffs. *In re United States*, Misc. No. 370, slip op. at 8 ("Egan is not distinguishable"); *In re United States*, Misc. No. 374, slip op. at 14 (lack of duty to disclose "all the clearer" when the information is contained in special access programs).

In this case, the Court's authority is even more limited. Plaintiffs' "superior knowledge" claims are based upon allegations of a judicially-created *implied* duty to disclose that *same* sort of "special access" information. It necessarily follows, from the rulings

by the court of appeals, that no such implied duty of disclosure may be imposed upon the Government in this case.

The "superior knowledge" doctrine involves the imposition, in limited circumstances, of a judicially-created, *implied* contractual obligation, derived from the more general implied obligation of a party not to hinder the other contracting party's performance. Plaintiffs do not (and cannot) allege that the Government actually "agreed" in this case to share special access information from other programs.[8] Instead, plaintiffs rely upon the notion that an obligation to share classified, special access information should be judicially imposed upon the Government, in contravention of the Executive's classification decisions made pursuant to Executive Order 12,356, sec. 4.2.

However, just as the Court may not "reverse special access decisions made by a service secretary under Executive Order 12356," *In re United States*, Misc. No. 374, slip op. at 8, plaintiffs may not dictate reversal of "special access decisions made by a service secretary" under the guise of alleging that the special access information constituted "superior

[8] Such an alleged implied-in-fact contract would be subject to a host of legal and factual deficiencies. For example, the very existence of the comprehensive A-12 FSED contract itself would preclude "implying" additional agreements regarding the parties' respective performance obligations. *Cf., ITT Federal Support Services v. United States*, 209 Ct. Cl. 157, 168 (1976); *Atlas Corp. v. United States*, 895 F.2d 745, 754 (Fed. Cir.), *cert. denied*, 111 S. Ct. 46 (1990).

knowledge" which the Government was under an implied contractual duty to share with contractors who had not been granted access to the programs in which the "superior knowledge" resided. The Government's general duty not to hinder performance cannot be stretched to encompass an implied duty to share classified military secrets with individuals not specifically authorized to receive those secrets.[9]

Because plaintiffs' claims are deficient as a matter of law, they should be dismissed.

B. Plaintiffs Have Not, And Cannot, Establish A *Prima Facie* Case

Plaintiffs have not made, and cannot make, a *prima facie* case that the Government possessed an implied contractual duty to share "superior knowledge" in this case, nor that the Government breached any such duty, for the simple reason that plaintiffs are wholly unable to address the four elements of a "superior knowledge" claim.

In order to prevail upon their "superior knowledge" claims, plaintiffs would have to establish each of the following elements:

[9] Moreover, cases have uniformly held that, even where the Government has a duty to share information, the Government need not automatically share all information in its possession, just because it may be helpful and/or unknown to the contractor. *E.g., Piasecki Aircraft Corp. v. United States*, 229 Ct. Cl. 222, 667 F.2d 50, 59 (1981); *Granite Construction Co. v. United States*, 24 Cl. Ct. 735, 751-52 (1991).

1. that plaintiffs undertook to perform without knowledge of a vital fact, in the possession of the Government, that affected performance;

2. that plaintiffs, in fact, did not possess the vital information from another source;

3. that the Government did not, in fact, supply the relevant information in some form, and the contractors merely failed to take steps to utilize the information at their disposal; and

4. that the Government was aware that the contractors had no knowledge of, or did not have a means to obtain, the information.

E.g., GAF Corp. v. United States, 932 F.2d 947, 949 (Fed. Cir. 1991), *cert. denied*, 112 S. Ct. 965 (1992). *See also, Lopez v. A.C. & S, inc.*, 858 F.2d 712, 717 (Fed. Cir. 1988), *cert. denied*, 491 U.S. 904 (1989); *American Ship Bldg. Co. v. United States*, 228 Ct. Cl. 220 (1981).

Even viewing the various submissions by plaintiffs in the most favorable light possible, it is patently apparent from the entire record in this case that plaintiffs attempt to address only, at most, the first element above.[10] Plaintiffs have consistently

[10] Plaintiffs have not expressly stated that they have established a *prima facie* case. In their memorandum of May 26, 1993, plaintiffs instead asked for further discovery in order to *attempt* to gather information to make out a *prima facie*

attempted to undertake discovery in order to determine whether some information somewhere might have existed which, in retrospect, could have helped them to perform. Of course, they cannot conduct this discovery because the matters which they seek are subject to the military state secrets privilege. Thus, plaintiffs' claims of "superior knowledge" must be dismissed, because the military

case. Moreover each declaration submitted by plaintiffs addressed only the *first* of the four elements of "superior knowledge" claim -- whether the Government held allegedly "vital" information. For example, plaintiffs' own memorandum, at page 5, states that Ross Williams' declaration "outlines how information from (the F-117A) program could have benefitted the A-12 program." That declaration relates only to whether plaintiffs lacked vital information. Similarly, the declaration of Ronald Hancock alleges only how information from the B-2 program would have altered the plaintiffs' cost proposals in the A-12 program. *See* 5/26/93 Memorandum, at 5. The declaration of Wayne Crouch, which is based upon his "recollection" of program documents, alleges that the B-2 and F-117A programs encountered problems "similar" to those encountered in the A-12 program, which again goes only to the first element of the "superior knowledge" test. Albert P. Farr's declaration concludes, at 15, that the B-2 and F-117A programs contained "vital information" for the A-12 program, including "vital schedule information," and weight, technical, and manufacturing information that would have been "of vital use" to the A-12 team. Finally, Dr. Keith Jackson's declaration similarly focuses only upon whether the information in the other programs "would have aided the contractors during performance of the contract" – *i.e.*, whether it was "vital" to the contractors. *See* Jackson Declaration ¶ 8. All of these declarations, then, address only one element of a superior knowledge claim. Such allegations, even if true, are meaningless by themselves, and insufficient to make out a *prima facie* case.

state secrets privilege precludes them from establishing, among other things, the nature of the information which the Government possessed.

C. The Very Fact That Plaintiffs' Claims Are "Inextricably Intertwined" With State Secrets Requires Dismissal.

It is not necessarily true that the party bearing the burden of proof always loses when invocation of the military state secrets privilege forecloses litigation of an issue, and the Government has not so agreed in this case. *See* 11/1/93 Order at 11-12. Rather, the parties appear to have agreed upon the correct principle: when a claim is so "inextricably intertwined with privileged matters" that it cannot be litigated, the claim must be dismissed. *Guong v. United States*, 860 F.2d 1063, 1066 (Fed. Cir. 1988), (*quoting Fitzgerald v. Penthouse International. Ltd.*, 776 F.2d at 1243 n. 11), *cert. denied*, 490 U.S. 1023 (1989).

As we pointed out at pages 10-11 of our most recent submission on this issue, one of the clearest statements of this proposition may be found in *Bareford v. General Dynamics Corp.*, 973 F.2d 1138 (5th Cir. 1992), *cert. denied*, 113 S. Ct. 1843 (1993), wherein the court held that a claim must be dismissed if "the very subject matter" of the claim involves a state secret. *Id.*, 973 F.2d at 1141, 1143-44. *See* 6/11/93 Def. Resp. to Pl. Motion for Continuance, at 10-11. Plaintiffs (in other circumstances) have expressly concurred:

> In summary, the circuits agree that dismissal is appropriate and necessary under *Reynolds* and *Totten at any stage in the litigation* when it becomes clear that plaintiffs cannot prove their prima facie case without classified information, **or the very subject matter of the litigation is privileged and further litigation would inevitably endanger secrets of state.**

Respondents' (General Dynamics') Brief in Opposition to Certiorari at 11, (S. Ct. No. 92-1209) (underscore in original; boldface supplied), App. 15.[11]

This statement of the law is correct, and application of that principle to this case conclusively establishes that dismissal of plaintiffs' "superior knowledge" claims is required. As we previously demonstrated at some length, *see* 5/27/93 Defendant's Motion to Dismiss at 13-22, and as the Court has correctly determined, *e.g.*, 11/1/93 Order at 10-11, the very nature of plaintiffs' claims in this case involve state secrets. The law in circumstances

[11] If plaintiffs had more candidly recognized the principles that they argued in *Bareford*, at least one trip to the court of appeals in this action might have been avoided. In *Bareford*, General Dynamics acknowledged the procedural correctness of an invocation of the military state secrets privilege that was materially indistinguishable from the invocation by Acting Secretary Donley challenged by plaintiffs in this case. Plaintiffs, of course, were correct in *Bareford*, and wrong in this case. *In re United States*, Misc. No. 374 (Fed. Cir., April 30, 1993).

such as the present is overwhelming plaintiffs' superior knowledge claims must be dismissed. *E.g.*, *Guong v. United States*, 860 F.2d at 1066-67; *see also*, *Weinberger v. Catholic Action*, 454 U.S. 139, 147 (1981); *Totten v. United States*, 92 U.S. 105 (1876); *Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1141 (5th Cir. 1992), *cert. denied*, 113 S. Ct. 1843 (1993); *Bowles v. United States*, 950 F.2d 154, 156 (4th Cir. 1991); *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 54748 (2d Cir. 1991); *Fitzgerald v. Penthouse International, Ltd.*, 776 F.2d 1236 (4th Cir. 1985); *Salisbury v. United States*, 690 F.2d 966, 977 (D.C. Cir. 1982); *Farnsworth Cannon. Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (*en banc*).

D. Plaintiffs Possess, And Cannot Carry, The Burden Of Establishing Their Superior Knowledge Claims

Plaintiffs' "superior knowledge" claims must be dismissed, regardless of any "burden of proof" analysis or arguments, because those claims are inextricably intertwined with state secrets.

Nevertheless, analysis of the respective burdens of proof also compels dismissal. Plaintiffs' superior knowledge claims are: (1) an affirmative defense to the Government's default termination, and (2) a claim that the Government materially breached the A-12 contract.[12] In both cases, plaintiffs

[12] Plaintiffs themselves repeatedly and consistently refer to their superior knowledge claim as a "defense" to the default termination. *E.g.*, 5/26/93 Pl. Mem. Concerning Continuation of Discovery at 3, 13.

bear the burden of establishing the existence of the Government's implied duty to share "superior knowledge," and the breach of that duty. Because those claims cannot be litigated in these circumstances, plaintiffs cannot satisfy their burdens. Accordingly, pursuant to any theory, plaintiffs' "superior knowledge" claims must be dismissed.

It is difficult to imagine a more obviously true proposition than the notion that a contractor bears the burden of proving asserted defenses to a termination for default, including an alleged breach of contract. This is confirmed by specific authorities addressing default terminations and affirmative defenses.

The Government bears the burden of establishing that the termination for default was appropriate, and will carry that burden in this case by showing, *inter alia,* that the A-12 was behind schedule and over-weight. *Lisbon Contractors. Inc, v. United States,* 828 F.2d 759, (Fed. Cir. 1987). The Government's burden does *not,* however, extend to affirmative defenses offered by a contractor, and especially to any alleged governmental contract breach offered as a "defense." *Id.* at 765 n.9 ("It must be noted that the contractor here asserted no affirmative defense, such as excusable delay. Our opinion does not encompass such matters.").

In specific cases where "superior knowledge" claims have been asserted as defenses to default terminations, courts and boards have *consistently* placed the burden of proof upon the contractor. *E.g.*,

Piasecki Aircraft Corp. v. United States, 667 F.2d 50, 59-60, 229 Ct. Cl. 208, 223 (1981) (default proper where "plaintiff had failed to establish" elements of superior knowledge claim); *H. N. Bailey & Associates v. United States*, 449 F.2d 376, 381, 196 Ct. Cl. 156, 175 (1971) (default sustained where "plaintiff was unable to introduce any evidence" to establish elements of superior knowledge claim); *Pauluhn Electric Mfg. Co., Inc.*, ASBCA No. 38130, 90-1 BCA ¶ 22,351 at 112,308 (1989); *Preston-Brady Co.. Inc.*, VABCA No. 1849, 86-2 BCA¶ 18,860 at 95,069 (1986); *Jet Power, Inc.*, ASBCA No. 21559, 83-1 BCA ¶ 16,516 at 82,069 (1983).[13]

Plaintiffs' superior knowledge claim is "an affirmative defense and, therefore, the party raising the defense, in this case [the plaintiffs], bears the burden of proof." *Nuss v. Office of Personnel Management*, 974 F.2d 1316, 1318 (Fed. Cir. 1992), *citing*, *A.C. Auckerman Co. v. R.L. Chaides Const. Co.*, 960 F.2d 1020, 1032 (Fed. Cir. 1992) (*in banc*); *Cornetta v. United States*, 851 F.2d 1372, 1380 (Fed. Cir. 1998) (*in banc*). Innumerable termination for default cases have made clear that the general burden of establishing all affirmative defenses to a default termination remains upon the contractor. *E.g.*, *United States v. Human Resources Management, Inc.*, 745 F.2d 642, 647 (Fed. Cir. 1984)

[13] *See also, Continental Rubber Works*, ASBCA No. 22447, 80-2 BCA ¶ 14,754 at 72,831 (1980); *Campeau Tool & Die Co.*, ASBCA No. 18436, 76-1 BCA ¶ 11,653 at 55,617-18 (1975); *Quality Controlled Stamping, Inc.*, ASBCA No. 19074, 74-2 BCA ¶ 10,757 at 51,149-50 (1974); *Jay-Rock Precision. Inc.*, ASBCA No. 17226, 72-2 BCA ¶ 9753 at 45,564 (1972).

("To the extent these facts might excuse [the contractor's] breach [resulting in default termination], [the contractor] had the burden of proof on this defense."); *Koppers Co., Inc. v. United States*, 405 F.2d 554, 563, 186 Ct. Cl. 142, 158-59 (1968) ("If performance was not possible, plaintiff's default is excused. The burden of proof on this issue is plaintiff's."); *J. Parr Construction v. United States*, 24 Cl. Ct. 228, 235 (1991) ("[p]laintiff bears the burden of proof' on its defense that differing site conditions justified its nonperformance), *aff'd*, 996 F.2d 319 (Fed. Cir. 1993) (table); *Norwood Mfg., Inc. v. United States*, 21 Cl. Ct. 300, 309 (1990) (contractor bore the burden of establishing its defenses of alleged erroneous specifications ("plaintiff did not show. . ."), abuse of discretion ("[p]laintiff must satisfy a significant burden of proof . . ."), and bad faith ("[p]laintiff must meet a high burden . . .")), *aff'd*, 930 F.2d 38 (Fed. Cir. 1991) (table)[14].

The burden of proof consistently has been placed upon a party alleging and relying upon a breach of the implied contractual duty to share

[14] Although plaintiffs will no doubt argue otherwise, the Government is not in the position to have particular knowledge of the facts regarding a "superior knowledge" claim, and no reported "superior knowledge" case has *ever* held that the Government generally bears the burden of proof on such a claim. Moreover, such an argument does not stand up to scrutiny. The contractor is in the best position to ascertain the effects of the alleged breach upon its own performance, and the "superior" knowledge of the Government becomes relevant only to the extent that it would have affected the contractor's performance.

superior knowledge. *E.g., GAF Corp. v. United States,* 932 F.2d 947, 949 (Fed. Cir. 1991), *cert. denied,* 112 S. Ct. 965 (1992); *Lopez v. A.C. & S., Inc.*, 858 F.2d 712, 717 (Fed. Cir. 1988), *cert. denied,* 491 U.S. 904 (1989).[15] No case has ever held that a defendant must dis-prove a breach of contract upon which the plaintiff seeks to rely -- that notion is absurd.

The applicable authorities conclusively demonstrate that plaintiffs bear the burden of establishing their "superior knowledge" defense. Plaintiffs' anticipated argument that the Government should bear the burden to dis-prove plaintiffs' superior knowledge claims is truly extraordinary, unprecedented, and unsupportable. Any burden of proof analysis compels dismissal of plaintiffs' claims.

[15] *Petrochem Services, Inc. v. United States,* 837 F.2d 1076 (Fed. Cir. 1988), is not to the contrary, but holds that in those rare cases in which the Government is attempting to rebut an allegation that it failed to transmit "superior knowledge" by showing that it did, in fact, orally convey that knowledge to the contractor, the Government must show that the oral communication was understood. *Petrochem* is, thus, consistent with the innumerable authorities confirming that contractors bear the burden of establishing all elements of an alleged breach of an implied duty to share superior knowledge.

E. The Rule Requiring Dismissal In These Circumstances Is Right, Equitable, And Appropriate

The necessary dismissal of plaintiffs' "superior knowledge" claims is fully in accord with established principles. To the extent that such a dismissal in this case presents an apparent inequity, the greater underlying interests reflected in the rule of law, national security, constitutional separation of powers, and the utility of the judicial process must prevail.

As we have previously noted: (1) even pursuant to the most charitable assumptions regarding plaintiffs' claims, dismissal in this case is not distinctly or atypically severe; (2) the authorities conclusively hold that the Government should not, and cannot, be made to "pay" for asserting the state secrets privilege in the civil context; and (3) common sense requires application of the rule mandating dismissal of plaintiffs' claims.

These specific plaintiffs, and large defense contractors generally, have quite often benefited from the Government's invocation of the state secrets privilege. *E.g.*, *Bareford v. General Dynamics Corp.*, 973 F.2d 1138 (5th Cir. 1992), *cert. denied*, 113 S. Ct. 1843 (1993); *Zuckerbraun v. General Dynamics Corp.*, 935 F. 2d 544 (2d Cir. 1991). *Bareford* and *Zuckerbraun* were wrongful death actions against the manufacturers of missile defense systems aboard a Navy vessel, including General Dynamics. The vessel was hit by Iraqi missiles in 1987, and the *Bareford* and *Zuckerbraun* plaintiffs alleged, *inter*

alia, that the contractors' negligence in the production and design of the missile defense systems were the proximate cause of the deaths of crewmen. The Government asserted the state secrets privilege regarding the facts relating to the production and design of the defense systems, and upon that basis the contractors successfully moved for dismissal. In this type of case, these contractor plaintiffs profit from the dismissal of colorable, and perhaps meritorious, claims by seriously and undeniably injured private parties. Any apparent inequity in these cases gives way to the rule of law, and to the greater interests underlying national security, constitutional separation of powers, and the utility of the judicial process.

The present case may be different in degree, but not in kind.[16] For all of the reasons that we have previously explained, plaintiffs' "superior knowledge" claims are legally and factually baseless. Accordingly, dismissal of those claims because they are intertwined with state secrets, or for any other reason, represents absolutely no unfairness or inequity at all. Nevertheless, even if one were to assume, contrary to the facts and law, that these

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[16] Despite the large number of dollars claimed by these contractors, the plaintiffs in *Bareford* and *Zuckerbraun* would no doubt contend that the stakes in their cases were higher than this one. Those plaintiffs were suing not upon a purely commercial contract dispute, but were instead seeking to vindicate the alleged wrongful deaths of their loved ones. Even if equitable or fairness concerns in specific cases could somehow outweigh controlling principles of law, it is by no means clear that this lawsuit would present the most compelling circumstance for such a renunciation of binding precedent.

contractor plaintiffs were losing a possibly meritorious claim, that loss would be no different than the loss these contractor plaintiffs themselves imposed upon the private parties in *Bareford* and *Zuckerbraun*.

Moreover, dismissal of plaintiffs' claims is consistent with the rule that the Government cannot be made to "pay" for the invocation of the state secrets privilege in civil actions in which it is a party. It is well established that the effect of the privilege is the "same," whether or not the Government is a party to the litigation. *E.g.*, *In re United States*, 872 F.2d at 476 ("Notions of sovereign immunity preclude . . . adverse consequence to the government, such as alteration of procedural or substantive rules"), *citing*, *Ellsberg v. Mitchell*, 709 F.2d 51, 65 (1983) ("the effect is the same, in other words, as if the government were not involved in the controversy"), *cert denied*, 465 U. S. 1038 (1984); *Salisbury v. United States*, 690 F. 2d 966, 976 (D.C. Cir. 1982); *Pan American World Airways, Inc. v. Aetna Casualty & Surety Co.*, 368 F. Supp. 1098, 1139 (S.D.N.Y. 1973), *aff'd*, 505 F.2d 989 (2d Cir. 1974); *Sigler v. LeVan*, 485 F. Supp. 185, 192-95 (D. Md. 1980); *Kinoy v. Mitchell*, 67 F.R.D. 1, 15 n. 50 (S.D.N.Y. 1975). Indeed, the invocation of the state secrets privilege is, essentially, a sovereign act. It is fundamental that the Government cannot be held liable for acts that it takes as a sovereign. *E.g.*, *Horowitz v. United States*, 267 U.S. 458, 461 (1924); *Atlas Corp. v. United States*, 895 F.2d 745, 754 (Fed. Cir. 1990).

In *Attorney General v. Irish People, Inc.*, 684 F.2d 928, 931 (D.C. Cir. 1982), *cert. denied*, 459 U.S. 1172 (1983), the court of appeals described several factors that should be considered before dismissal of any claim by the Government, *all* of which proscribe the imposition of any sanction against the Government in this case. Specifically, the privileged information is not likely to exculpate plaintiffs -- the nature of the privileged information, in fact, includes matters that could provide a complete defense *for the Government* to plaintiffs' "superior knowledge" claims. Plaintiffs have no overriding necessity for their attenuated, ancillary excuse of "superior knowledge," nor is the loss of a single, legally-deficient excuse fatal to plaintiffs' ability to present their position concerning their A-12 performance failures. The Government's interest in maintaining the secrecy of its most valuable military secrets, and in successfully retaining the ability to enforce contracts for defense-related goods and services, is paramount. In attempting to allow plaintiffs to develop their legally baseless "superior knowledge" excuse until it became apparent that that would not be possible, the Government has exhibited extraordinary cooperation. Rather than sanctioning the Government for protecting national security, this case could simply become focused upon what should be at issue, namely plaintiffs' performance failures under the A-12 contract. *See Irish People*, 684 F. 2d at 951.

Finally, common sense demands the rejection of any assertion by plaintiffs that the elimination of their novel "superior knowledge" claims should

somehow preclude the Government from prevailing upon the entire default termination. Pursuant to such a view, *every* terminated defense contractor could make a claim that the Government failed to share information contained in secret, unacknowledged programs. The Government would then be forced either to disclose the existence and substance of the programs to defend itself, or lose its ability to terminate contractors for default.[17] That, of course, cannot be the law. The Government's ability to insist upon performance of contracts for the procurement of defense-related goods and services would be eviscerated. Moreover, such a view would eliminate the ability of the Executive to control access to military and diplomatic matters, in clear violation of constitutional proscriptions, *e.g.*, *Department of the Navy v. Egan*, 484 U.S. 518, 527-28 (1988), and would impose an automatic penalty upon the Government for invoking the state secrets privilege, in violation of settled principles. *E.g.*, *In re United States*, 872 F.2d at 476; *Ellsberg*, 709 F.2d at 65.

[17] Similarly, findings in favor of a contractor who manages to frame a claim that implicates state secrets, or who manages to convince a court that it has made a *prima facie* showing upon such a claim, would "provide every incentive to probe dangerously close to state secrets themselves." *Farnsworth Cannon, Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (*en banc*). The long-term detrimental effects of such a ruling would be incalculable.

CONCLUSION

For the reasons stated above, we respectfully request that the Court dismiss plaintiffs' "superior knowledge" claims.

Respectfully submitted,

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November 19, 1993

* * * *

No. 91-1204C
(Judge Hodges)

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,

Plaintiffs,

v.

THE UNITED STATES,

Defendant.

DEFENDANT'S OPPOSITION TO PLAINTIFF'S MOTION FOR SUMMARY JUDGMENT ON COUNT IX, AND MOTION TO DISMISS OR IN THE ALTERNATIVE CROSS MOTION FOR SUMMARY JUDGMENT

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IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DEFENDANT'S OPPOSITION TO PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT ON COUNT IX, AND MOTION TO DISMISS OR IN THE ALTERNATIVE CROSS MOTION FOR SUMMARY JUDGMENT

Plaintiffs' Motion for Summary Judgment on Count IX, dated November 22, 1993, in fact establishes that plaintiffs' "superior knowledge" claims must be dismissed. Plaintiffs are correct in recognizing that their claims must be resolved upon dispositive motions, but they err in asserting that the circumstances and controlling authorities allow judgment in their favor.

Plaintiffs' superior knowledge claims are inextricably intertwined with information that is protected by the military state secrets privilege. As

we demonstrate with these submissions, most of plaintiffs' proposed findings of "uncontroverted" fact are, actually, "controverted" by the current record in this case. Yet, it is simply not possible for the Court to resolve these issues, in light of the affirmed assertion of the state secrets privilege in this case, the nature of plaintiffs' claims, and the nature of the information that would be required for litigation of these matters. Moreover, the Government is precluded from demonstrating its defenses to plaintiffs' claims. Accordingly, those claims must be dismissed.

In addition, although the parties are now years into this litigation, it has become increasingly apparent that plaintiffs' claims diverge radically from any recognized notion of the "superior knowledge" doctrine. In other words, not only is the very subject matter of plaintiffs' claims a state secret, those claims, themselves, are legally deficient. Plaintiffs have not made, and cannot make, a *prima facie* showing of the existence or breach of the implied duty upon which they rely, and can cite no authority for their argument that the Government bears the burden of proof in these circumstances.

In short, there is no authority that would support entry of judgment for plaintiffs. The law requires dismissal of plaintiffs' "superior knowledge" claims.

* * * *

SUMMARY OF THE ARGUMENT

Plaintiffs' "superior knowledge" claims are inextricably intertwined with information that is subject to the military state secrets privilege. Further litigation of those claims would inevitably endanger national security and threaten disclosure of state secrets. The authorities conclusively establish that in such circumstances plaintiffs' claims must be dismissed.

Plaintiffs' new, revised characterization of their claims as not encompassing specific, classified special access information falls far outside of the "superior knowledge" doctrine, contradicts the allegations in their complaint, and is ultimately meaningless.

Finally, plaintiffs undeniably possess, and cannot carry, the burden of proof upon their "superior knowledge" defense, and are not entitled to a judgment in their favor because the Government has invoked the state secrets privilege.

ARGUMENT

Plaintiffs' motion reveals that they want everything both ways. They want the Court to find: (1) that they have proved their case, P. Br. 7-18, but that they cannot prove their case, P. Br. 40; (2) that the Government conclusively invoked the state secrets privilege, P. Br. 35-42, but that the Government did not properly invoke the privilege, P. Br. 19; (3) that the Court should decide the case on

the basis of the incomplete evidence already produced, P. Br. 22, but that the Court must base its decision on all of the relevant facts, P. Br. 29 n.13; and (4) that plaintiffs should prevail if the Government challenges their purported *prima facie* showing, P. Br. 39 n.19, and that plaintiffs should prevail if the Government does not challenge that purported showing. P. Br. 22.

Plaintiffs' dizzying effort to be on all sides of every position, however, does not alter the ineluctable proposition upon which the disposition of this matter turns. That proposition is, ultimately, very simple: plaintiffs' "superior knowledge" claims are inextricably intertwined with state secrets, and must therefore be dismissed.

I. Plaintiffs' Superior Knowledge Claims Must Be Dismissed Because They Are "Inextricably Intertwined" With State Secrets

In the hundreds of pages of briefs that the parties have filed on these issues in this case, plaintiffs have steadfastly refused to squarely address the one legal principle that is dispositive -- dismissal of a claim is required where the very subject matter of the claim is privileged, and further litigation would inevitably endanger secrets of state. Plaintiffs' failure to address this principle is particularly curious, given that one of these plaintiffs

successfully propounded that precise argument to other courts in other cases.[6]

A. The Authorities Require Dismissal Of Plaintiffs' Claims

As we previously demonstrated and describe further below, the very nature of plaintiffs' claims in this case involve state secrets. *See* 5/27/93 Defendant's Motion to Dismiss at 13-22, *cf.*, 11/1/93 Order at 10-11. In such circumstances, the authorities overwhelmingly require dismissal of plaintiffs' claims. *E.g., Guong v. United States*, 860 F.2d at 1066-67; *see also, Weinberger v. Catholic Action*, 454 U.S. 139, 147 (1981); *Totten v. United States*, 92 U.S. 105 (1876); *Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1141 (5th Cir. 1992),

[6] *See* Respondents' (General Dynamics') Brief in Opposition to Certiorari at 11, (S. Ct. No. 92-1209) ("dismissal is appropriate and necessary under [*United States v.*] *Reynolds* [354 U.S. 1 (1953)] and *Totten* [*v. United States*, 92 U.S. 105 (1876)] *at any stage in the litigation* when it becomes clear that plaintiffs cannot prove their prima facie case without classified information, **or the very subject matter of the litigation is privileged and further litigation would inevitably endanger secrets of state**.") (underscore in original, boldface supplied). At pages 19-20 of plaintiffs' recent brief in opposition to the Government's motion to dismiss, dated December 17, 1993, plaintiffs make an incorrect and unsupportable assertion that privileged information is not inextricably intertwined with their claims. As the Acting Secretary of the Air Force has stated, and as the Court has held, plaintiffs are wrong. *See* 7/22/93 McPeak Decl. ¶ 10; *e.g.*, 3/18/93, 5/7/93 Orders (information "relevant"); 3/31/93 and 4/12/93 Orders (information "crucial"). We intend to reply separately to plaintiffs' December 17, 1993 filing.

cert. denied,113 S. Ct. 1843 (1993); *Bowles v. United States*, 950 F.2d 154, 156 (4th Cir. 1991); *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 547-48 (2d Cir. 1991); *Fitzgerald v. Penthouse International. Ltd.*, 776 F.2d 1236 (4th Cir. 1985); *Salisbury v. United States*, 690 F.2d 966, 977 (D.C. Cir. 1982); *Farnsworth Cannon, Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (*en banc*).

Every factor that mandated dismissal in each of these cases is similarly present here. For example, in *Zuckerbraun*, the then-Secretary of the Navy: (1) invoked the state secrets privilege with regard to certain information; (2) described his understanding of the subject matter of claims in the lawsuit; (3) described the classified nature of the information that would be required to resolve those claims; and (4) conveyed his conclusion that trial of those matters would unavoidably call for information which is classified and subject to the military state secrets privilege. *Id.*, 935 F.2d at 548-553. In this case, the Acting Secretaries of the Air Force have: (1) invoked the state secrets privilege, *e.g.*, 3/30/93 Donley Decl.; (2) described the subject matter of the claims in this lawsuit, *see* 7/22/93 McPeak Decl. ¶¶ 7-13, 3/30/93 Donley Decl. ¶ 19; (3) described the classified nature of the information that would be required to resolve those claims, *see* 7/22/93 McPeak Decl. ¶¶ 3-4, 7-8; 3/30/93 Donley Decl. ¶ 12-13, 19; and (4) conveyed the conclusion that trial of those claims would unavoidably call for information which

is classified and subject to the military state secrets privilege. 7/22/93 McPeak Decl. ¶¶ 12-13.[7]

The authorities conclusively establish that in these circumstances plaintiffs' "superior knowledge" claims must be dismissed.

B. The Record In This Case, And Plaintiffs' Motion, Conclusively Establish That The Very Subject Matter Of Plaintiffs' Claims Is A State Secret

i. There Are Factual Issues That Cannot Be Resolved In This Case

As established in more detail in the Government's Responses to Plaintiffs' Proposed Findings of Uncontroverted Fact, evidence in the current record contradicts virtually every material fact that plaintiffs seek to have the Court find.

For example, plaintiffs were actually involved in, and therefore fully aware of, the development of

[7] Plaintiffs' citation to *Molerio v. Federal Bureau of Investigation*, 749 F.2d 815 (D.C. Cir. 1984), further demonstrates that dismissal of plaintiffs' claims is required. As plaintiffs acknowledge, even though there may have been "circumstantial evidence to support" plaintiffs' claims in *Molerio*, the Government's "invocation of the state secrets doctrine precluded the [Government] from asserting a valid defense." P. Br. 42. That is *precisely* the situation here -- the Government is precluded from asserting its defenses to plaintiffs' claims, because those defenses, and the claims themselves, are inextricably intertwined with privileged matters.

the B-2 program prior to the commencement of the ATA (A-12) competition, and they were aware that the B-2 and F-117A programs were well underway. *E.g.*, GRPPF No. 2-3; Ex. 19 (Air Force Independent Review Team Report, dated August 15, 1989, at 6-7). Plaintiffs fully participated in the development of the "knowledge base" that gave rise to their A-12 design, and plaintiffs ensured that the Government was aware of plaintiffs' extensive knowledge. *E.g.* GRPPF No. 3, Ex. 4 (BAFO excerpts). Because of plaintiffs' prior experiences, the prior heavy Government investment in the development of low observable technology in these two companies, and, perhaps most importantly, plaintiffs' own representations to the Government regarding their anticipated acquisition and/or development of any low observable information that they might require, at the time of contract award the Government could not have known of any alleged need by plaintiffs for additional information. *E.g.*, GRPPF Nos. 3, 10, 11, 12, 15, 16, 18, 23, 27 and materials cited therein.

Moreover, during the course of the project, the plaintiffs affirmatively and deliberately refused to take advantage of the Government's efforts to provide warnings and information from other programs. This refusal appears to have been based upon plaintiffs' desire to pursue their competition against each other in the ATF (F-22) competition. *E.g.*, GRPPF Nos. 6, 19, 24; Ex. 19 (Maj. March November 20, 1990 Memorandum). In effect, each of these contractors implicitly agreed to sacrifice progress on the A-12 project, because they did not

want to help the other contractor win the ATF competition. Indeed, plaintiffs exercised voluntary self-denial of information between and within their own corporations, for competitive reasons. *E.g.* GRPPF Nos. 5 and 27; P. Ex. 23 (CAIG report, at 3); Ex. 3 (Snodgrass letter, dated January 8, 1987). In addition, if plaintiffs truly lacked any F-117A information, it was not because of a Government failure to warn, but, rather, because plaintiffs determined not to provide the compensation to Lockheed necessary to secure such knowledge. *See* P. Ex. 4 (11/19/93 Jackson Decl. ¶ 20-22); Ex. 12 (Lamers memorandum, dated March 12, 1988).

In sum, there is more than sufficient evidence in the record such that a finder of fact reasonably could conclude that: (1) prior to award, the Government did not know that plaintiffs would need information from other special access programs; (2) the Government attempted to provide warnings to plaintiffs; (3) the Government attempted to disclose the "knowledge" that the contractors now allege was not shared; (4) the allegedly withheld information was more than reasonably available to plaintiffs (and, in all probability, actually in their possession), and; (5) plaintiffs were not misled.

One part of plaintiffs' motion is dependent upon findings contrary to the above. Because the facts and evidence are vigorously disputed upon the current record, however, such findings are not permissible. *E.g.* RCFC 56(e); *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 249-51, 257 (1986). The Government has more than come forward with

specific showings of genuine material factual issues in dispute. *E.g., Celotex Corp. v. Catrett*, 477 U.S. 317, 324 (1986). To the extent that more than one inference may be drawn from the materials before the Court, all doubts must be resolved in favor of the Government. *E.g., Litton Indus. Prods, inc. v. Solid State Sys. Corp*, 755 F.2d 158, 163 (Fed. Cir. 1985).

Moreover, resolution of these issues cannot occur without exploration of information that is subject to the absolute military state secrets privilege -- these matters are inextricably intertwined with state secrets. In other words, not only are there factual issues, there are factual issues that cannot be resolved in this case. In such circumstances, dismissal of plaintiffs' claims is required.

ii. The Continuing And Inevitable Security Incidents In This Case Confirm The Non-Justiciability Of Plaintiffs' Claims

The proposition that further litigation of plaintiffs' superior knowledge claims would cause the disclosure of military secrets is not purely theoretical. In fact, in this case already there have been everal instances of possible disclosure or reference to privileged state secrets. These incidents have occurred, despite the best efforts of all individuals involved, because plaintiffs have continued aggressively to pursue their claims since the invocation of the privilege and the Government's associated motion to dismiss.

The current significance of these incidents lies not in apportioning blame or imposing sanctions or adverse findings -- that goes beyond the scope of the issues before the Court.[8] Rather, the significance of these incidents is to confirm that the very nature of plaintiffs' claims is unavoidably, inextricably intertwined with privileged state secrets. *See* 7/22/93 McPeak Decl. ¶¶ 12-13. Relatively straightforward questions, including questions that *must* be asked and answered to resolve any "superior knowledge" claim, cannot be resolved in this case. *See* 7/22/93 McPeak Decl. ¶ 10. Plaintiffs have so admitted. *E.g.*, 12/7/93 Motion to Strike at 6. On multiple occasions, this Court itself has noted that the privileged information is "relevant," *e.g.*, 3/18/93 Order; 5/7/93 Order, and that the privileged material is "crucial" to the resolution of plaintiffs' superior knowledge case. *E.g.*, 3/31/93 Order; 4/12/93 Order; 4/14/93 Order.

The record in this case is conclusive. The attempted litigation of plaintiffs' "superior

[8] Our submissions dated November 19, 1993, provided additional factual detail regarding several of these matters, and re-emphasized our belief that no implied wrongdoing or impropriety upon the part of the Government would justify any negative inference by this Court. At a hearing on December 10, 1993, the Court expressed certain concerns, apparently based upon several misunderstandings between the Court and the Government. We continue to address these matters in separate filings. We note, however, that the primary reason for one concern that the Court expressed -- *i.e.*, Government lawyers investigating matters classified beyond the boundaries of the A-12 program -- would cease to exist upon the dismissal of plaintiffs' claims.

knowledge" claims would inevitably endanger secrets of state. Those claims must, therefore, be dismissed.

II. Plaintiffs' Claims Fall Far Outside Of The "Superior Knowledge" Doctrine

A. Plaintiffs' Assertion That The Government Breached A Duty To Share With Them Other Contractors' General Lack Of Success On Other Projects Is Unavailing, As A Matter Of Law

Plaintiffs propound inconsistent conceptions of their superior knowledge claims. In their complaint and portions of their brief, they claim that the Government failed to share "detailed low observable" information contained in other classified, special access programs. *E.g.*, Br. 15; Second Amended Unclassified Complaint ¶¶ 46, 269-74. At the same time, however, plaintiffs imply that they should have been notified in general terms that Northrop merely encountered "weight" and "schedule" problems on the B.-2 project. P. Br. 18. The latter assertions diverge widely from any recognized notion of the superior knowledge doctrine, and are ultimately meaningless.

The following statement of the law by this Court is instructive:

> So far as the court is aware, in no prior decision has the Government been held liable for failure to disclose the uniqueness of a similar earlier project, or a

> prior contractor's lack of success with a particular (and, in effect, experimental) methodology, or for lack of disclosure of relevant, albeit controverted reports. Instead, the clear import of the cases most nearly on point is to the contrary.

Granite Construction Co. v. United States, 24 Cl. Ct. 735, 751 (1991), *citing*, *American Ship Building Co. v. United States*, 228 Ct. Cl. 220, 654 F.2d 75 (1981); *Intercontinental Manufacturing Co. v. United States*, 4 Cl. Ct. 591 (1984). The Government need not automatically share all information in its possession, of course, just because it may be helpful and/or unknown to the contractor. *E.g.*, *Piasecki Aircraft Corp. v. United States*, 229 Ct. Cl. 222, 667 F.2d 50, 59 (1981).

Knowledge of the possible existence of a "schedule problem" or a "weight problem" is not "superior knowledge." Delays and weight overruns occur for specific *reasons*. Government identification of a mere "schedule problem" on a prior contract would act as nothing more than a general deterrent to bidders, which the Government clearly has no duty to provide. *E.g.*, *American Ship Building Co. v. United States*, 228 Ct. Cl. 220, 225-26 (1981) ("[I]t would be irresponsible procurement to seek to deter bidders from bidding, or even to seem to do so."). Even *J.A. Jones Construction Company v. United States*, 182 Ct. Cl. 615 (1968), upon which plaintiffs exclusively rely, involved a *specific* performance

problem, *i.e.*, a shortage of the local labor supply. Plaintiffs' failure to identify such a specific performance problem, years into this litigation, is telling and fatal. For this additional reason, plaintiffs' claims should be dismissed.

B. The Legal Duty Described In Plaintiffs' Complaint Cannot Be Implied In These Circumstances

The legal duty that plaintiffs allege the Government breached in their complaint cannot be implied in these circumstances.[9] This is because such an application of the "superior knowledge" doctrine would violate the Executive's exclusive constitutional responsibility to exercise its judgment and expertise, in determining with whom "special access" military secrets will be shared. *E.g.*, *Department of Navy v. Egan*, 484 U.S. 518 (1988); Executive Order 12,356 sec. 4.2 (April 2, 1982), 3 C.F.R. 166, 174 (1983).

The "superior knowledge" doctrine involves the imposition, in limited circumstances, of a judicially-created, *implied* contractual obligation, derived from the more general implied obligation of a party not to hinder the other contracting party's performance. Plaintiffs rely upon the notion that an obligation to share classified, special access

[9] *See also* Govt. Motion to Dismiss dated May 27, 1993; Govt. Brief dated November 19, 1993. The *reasons* for the "schedule" and "weight" problems that plaintiffs allege could have been avoided necessarily implicates *specific* information classified within other special access programs.

information should be judicially imposed upon the Government, in contravention of the Executive's classification decisions made pursuant to Executive Order 12,356, sec. 4.2.

However, just as the Court may not "reverse special access decisions made by a service secretary under Executive Order 12356," *In re United States*, Misc. No. 374, slip op. at 8, plaintiffs may not dictate reversal of "special access decisions made by a service secretary," under the guise of alleging that the special access information constituted "superior knowledge" which the Government was under an implied contractual duty to share with contractors who had not been granted access to the programs in which the "superior knowledge" resided. The Government's general implied duty not to hinder performance cannot be stretched to encompass an implied duty to share classified military secrets with individuals not specifically authorized to receive those secrets.

C. Plaintiffs Cannot Rely Upon An Implied-In-Fact Contract To Share Classified Information

Plaintiffs hint, but thus far do not expressly claim, that the Government in fact agreed to supply classified, special access information from other programs. *E.g.*, P. Br. 8; 11/18/93 Farr Decl. ¶¶ 31, 34 (P. Ex. 5). Such an allegation has nothing to do with the "superior knowledge" doctrine. *E.g.*, *GAF Corp. v. United States*, 932 F.2d 947, 949 (Fed. Cir. 1991) (elements of superior knowledge claim), *cert.*

denied, 112 S. Ct. 965 (1992). Rather, plaintiffs appear to rely upon an alleged actual understanding between the parties -- an implied-in-fact contract.

An implied-in-fact contract with the United States requires findings of: mutuality of intent to contract; consideration; lack of ambiguity in offer and acceptance; and actual authority of the Government agent whose conduct is relied upon to bind the Government. *E.g.*, *City of El Centro v. United States*, 922 F.2d 816, 820 (Fed. Cir. 1990); *Domaglia v. United States*, No. 92-883 (Ct. Fed. Cl., November 30, 1993), slip op. at 3. Moreover, the very existence of a comprehensive written contract precludes "implying" additional agreements regarding the parties' respective performance obligations, as a matter of law. *Cf.*, *ITT Federal Support Services v. United States*, 209 Ct. Cl. 157, 168 (1976); *Atlas Corp. v. United States*, 895 F.2d 745, 754 (Fed. Cir.), *cert. denied*, 111 S. Ct. 46 (1990).

It is patently apparent that plaintiffs cannot recover upon an implied-in-fact contract theory. For example, plaintiffs cannot identify any Government agent here who has authority to enter into a contract to share classified, special access information -- that authority is strictly circumscribed by Executive Order 12,356. Plaintiffs can point to no evidence of Government intent to enter such a contract, nor can they explain why, if the parties had an understanding regarding such an allegedly vital matter, the parties did not simply reduce that understanding to writing in the several hundred page agreement that they executed.

Plaintiffs' vague claims regarding what they allege the parties may have "understood" are insufficient as a matter of law, and provide no support for plaintiffs' position.

III. The Government's Invocation Of The State Secrets Privilege Does Not Entitle Plaintiffs To A Favorable Judgment

A. An Evidentiary Privilege Is Not A Breach Of The Disputes Clause Of The Contract

At pages 27-31 of their brief, plaintiffs argue that the Government's invocation of the military state secrets privilege in this case is a "breach" of the Government's contractual duties under the Disputes clause of the A-12 FSED contract. Plaintiffs, of course, can cite no authority that even remotely supports such a theory.[10] A brief examination of the implications of plaintiffs' argument further demonstrates its invalidity.

[10] *Moore-McCormack Lines, Inc. v. United States*, 188 Ct. Cl. 644, 413 F.2d 568 (1969), did not even involve claims regarding the Disputes clause of a contract, but, rather, a challenge to administrative determinations under "very special provisions" of the Merchant Marine Act of 1936. *Id.*, 413 F.2d at 576. *Nager Electric Co. v. United States*, 177 Ct. Cl. 234, 368 F.2d 847 (1966), merely held that administrative actions before an agency must be completed, before a statutory limitations period commences. Neither of these cases cited by plaintiffs have anything to do with contractual dispute resolution, evidentiary privileges, or a failure to produce information as a contractual "breach." Plaintiffs can cite no case in support of their novel theory.

First, there is nothing about plaintiffs' theory that limits its application to the state secrets privilege. Pursuant to plaintiffs' position, every sustained privilege assertion, including the attorney-client or any other privilege, would be a refusal to "disclose the information necessary to resolve 'all aspects of a dispute.'" P. Br. 29. Clearly, the Government does not intend to abrogate all of its valid evidentiary privileges when it enters a contract containing the standard Disputes clause.

Second, the logical implication of plaintiffs' argument is that the Disputes clause in every Government contract for procurement of defense-related goods and services reflects an agreement by the Government to disclose any and all information that might exist, even if the information is classified in other special access programs. Not only would the contracting entity likely lack authority to agree to such disclosure under Executive Order 12,356, but such an interpretation of the Disputes clause clearly cannot be the law. If plaintiffs' view were true, then *every* terminated defense contractor could make a claim that the Government failed to share information contained in secret, special access programs. The Government would then be forced either to disclose the existence and substance of the programs to defend itself, or lose its ability to terminate contractors for default. Such distortions of the Disputes clause and the Executive's right to control military secrets cannot be correct.

Third, plaintiffs' argument is fatally flawed for an even more fundamental reason -- there was

simply nothing to "breach" when the Government asserted the state secrets privilege in this litigation. Plaintiffs' argument is that because the Government itself allegedly breached the A-12 FSED contract the Government was not entitled to terminate that contract for default, P. Br. 24, and that the invocation of the state secrets doctrine in this litigation was such a "breach" of the Disputes clause. P. Br. 30. That asserted "breach," however, obviously occurred *years* after the contractual relationship between the parties had ended. There was no existing contract that could have been "breached" by the Government in March of 1993, when the privilege was formally invoked. The subsequent, post-termination privilege assertion by the Government in litigation cannot retroactively invalidate the Government's exercise of its contractual right to terminate the contract for default. Plaintiffs' improbable and unsupported argument to the contrary must be rejected.[11]

B. Plaintiffs Have Not, And Cannot, Establish A Prima Facie Case

Plaintiffs have not made, and cannot make, a *prima facie* case that the Government possessed an

[11] Plaintiffs' extensive discussions regarding the sovereign acts doctrine, P. Br. 31-35, are immaterial to these circumstances. While there are obvious parallels between the sovereign acts doctrine and the state secrets privilege -- automatic penalties cannot be imposed upon the Government in either circumstance, and both are driven by overriding concerns of national interest -- the state secrets doctrine is a distinct, evidentiary privilege.

implied contractual duty to share "superior knowledge" in this case, nor that the Government breached any such duty, for the simple reason that plaintiffs are wholly unable to meet the four elements of a "superior knowledge" claim.

In order to prevail upon their "superior knowledge" claims, plaintiffs would have to establish each of the following elements:

> 1. that plaintiffs undertook to perform without knowledge of a vital fact, in the possession of the Government, that affected performance;
>
> 2. that plaintiffs, in fact, did not possess the vital information from another source;
>
> 3. that the Government did not, in fact, supply the relevant information in some form, and the contractors merely failed to take steps to utilize the information at their disposal; and
>
> 4. that the Government was aware that the contractors had no knowledge of, or did not have a means to obtain, the information.

E.g., GAF Corp. v. United States, 932 F.2d 947, 949 (Fed. Cir. 1991), *cert. denied*, 112 S. Ct. 965 (1992). *See also, Lopez v. A.C. & S, inc.*, 858 F.2d 712, 717 (Fed. Cir. 1988), *cert. denied*, 491 U.S. 904 (1989); *American Ship Bldg. Co. v. United States*, 228 Ct. Cl. 220 (1981).

Even viewing the various submissions by plaintiffs in the most favorable light possible, it is patently apparent from the entire record in this case that plaintiffs address only, at most, the first element above.[12] Plaintiffs have consistently

[12] Each declaration submitted by plaintiffs addresses only the *first* of the four elements of "superior knowledge" claim -- whether the Government held allegedly "vital" information. For example, plaintiffs' 5/26/93 memorandum, at page 5, states that Ross Williams' 5/20/93 declaration "outlines how information from [the F-117A] program could have benefitted the A-12 program." That declaration relates only to whether plaintiffs lacked vital information. Similarly, the 5/23/93 declaration of Ronald Hancock alleges only how information from the B-2 program would have altered the plaintiffs' cost proposals in the A-12 program. *See* 5/26/93 Memorandum, at 5. The 5/25/93 and 11/18/93 declarations of Wayne Crouch allege that the B-2 and F-117A programs encountered problems "similar" to those encountered in the A-12 program, and that information from these programs "would have assisted" plaintiffs. Albert P. Farr's 5/25/93 declaration concludes, at 15, that the B-2 and F-117A programs contained "vital information" for the A-12 program, including "vital schedule information," and weight, technical, and manufacturing information that would have been "of vital use" to the A-12 team, and his 11/18/93 declaration repeats those allegations. Finally, Dr. Keith Jackson's declarations focus upon whether the information in the other programs "would have aided the contractors during performance of the contract" -- *i.e.*, whether it was "vital" to the contractors. *See* 5/25/93 Jackson Decl. ¶ 8. Similarly, Mr. Jackson's 11/19/93 declaration focuses upon the alleged existence of information in "other low observable . . . weapon system development programs," and upon the Government's alleged failure to share that information. All of these declarations, then, address only one element of a superior knowledge claim. Such allegations, even if true, are meaningless by themselves, and insufficient to make out a *prima facie* case.

attempted to undertake discovery in order to determine whether some information somewhere might have existed which, in retrospect, could have helped them to perform. Of course, they cannot conduct this discovery because the matters which they seek are subject to the military state secrets privilege. Thus, plaintiffs' claims of "superior knowledge" must be dismissed, because the military state secrets privilege precludes them from establishing, among other things, the nature of the information which the Government possessed.

C. Plaintiffs Possess, And Cannot Carry, The Burden Of Establishing Their Superior Knowledge Claims

At pages 37-38 of their motion, plaintiffs make an untenable argument that the Government bears the burden of dis-proving the contractual breach defense upon which plaintiffs rely. As we previously established in response to the Court's November 1, 1993 order, however, that argument is simply wrong.

Plaintiffs ignore: (1) the express limitation upon the burden-of-proof ruling stated by the court of appeals in *Lisbon Contractors, Inc. v. United States*, 828 F.2d 759 (Fed. Cir. 1987); and (2) the innumerable authorities holding that contractors have the burden of establishing defenses to default terminations generally, and "superior knowledge" defenses specifically.

In *Lisbon Contractors. Inc. v. United States*, 828 F.2d 759, (Fed. Cir. 1987), the court of appeals

explicitly disavowed the holding that plaintiffs attempt to ascribe to that decision:

> It must be noted that the contractor here asserted no affirmative defense, such as excusable delay. Our opinion does not encompass such matters.

Id., 828 F.2d at 765 n.9. Once again, plaintiffs want it both ways -- they want to be viewed as "defendants," but they do not want the Court to examine the necessary implications of their affirmative "defense" upon the allocation of the burden of proof. P. Br. 37.

In our November 19, 1993 brief, we noted that plaintiffs' superior knowledge claim is "an affirmative defense and, therefore, the party raising the defense, in this case [the plaintiffs], bears the burden of proof," *Nuss v. Office of Personnel Management*, 974 F.2d 1316, 1318 (Fed. Cir. 1992) (citations omitted). The cases uniformly hold that the contractor bears the burden of proof to establish defenses to a default termination. *E.g.*, *United States v. Human Resources Management. Inc.*, 745 F.2d 642, 647 (Fed. Cir. 1984); *Koppers Co.. Inc. v. United States*, 405 F.2d 554, 563, 186 Ct. Cl. 142, 158-59 (1968); *J. Parr Construction v. United States*, 24 Cl. Ct. 228, 235 (1991), *aff'd*, 996 F.2d 319 (Fed. Cir. 1993) (table); *Norwood Mfg., Inc. v. United States*, 21 Cl. Ct. 300, 309 (1990), *aff'd*, 930 F.2d 38 (Fed. Cir. 1991) (table).

Moreover, in circumstances precisely analogous to this one -- where the contractor asserts a "superior knowledge" defense to a default termination -- we demonstrated that courts consistently place the burden of establishing all elements of that defense upon the contractors. 11/19/93 Govt. Br. at 23-24. *See Piasecki Aircraft Corp. v. United States*, 667 F.2d 50, 59-60, 229 Ct. Cl. 208, 223 (1981) (default proper where "plaintiff had failed to establish" elements of superior knowledge claim); *H. N. Bailey & Associates v. United States*, 449 F.2d 376, 381, 196 Ct. Cl. 156, 175 (1971) (default sustained where "plaintiff was unable to introduce any evidence" to establish elements of superior knowledge claim); *Pauluhn Electric Mfg. Co., Inc.*, ASBCA No. 38130, 90-1 BCA ¶ 22,351 at 112,308 (1989); *Preston-Brady Co., Inc.*, VABCA No. 1849, 86-2 BCA ¶ 18,860 at 95,069 (1986); *Jet Power, Inc.*, ASBCA No. 21559, 83-1 BCA ¶ 16,516 at 82,069 (1983).[13] This is consistent with the indisputable proposition that it is the contractor that bears the ultimate burden of proof when it alleges that the Government breached an implied duty to share superior knowledge. *E.g., GAF Corp. v.*

[13] *See also, Continental Rubber Works*, ASBCA No. 22447, 80-2 BCA ¶ 14,754 at 72,831 (1980); *Campeau Tool & Die Co.*, ASBCA No. 18436, 76-1 BCA ¶ 11,653 at 55,617-18 (1975); *Quality Controlled Stamping, Inc.*, ASBCA No. 19074, 74-2 BCA ¶^E^E^E 10,757 at 51,149-50 (1974); *Jay-Rock Precision, Inc.*, ASBCA No. 17226, 72-2 BCA ¶ 9753 at 45,564 (1972).

United States, 932 F.2d 947, 949 (Fed. Cir. 1991), *cert. denied*, 112 S. Ct. 965 (1992).[14]

Plaintiffs do not directly address these authorities and principles, nor the Court's observation that the "party bearing the burden of proof on the superior knowledge issue cannot prevail." 11/1/93 Order at 12. That party is indisputably plaintiffs. Any burden of proof analysis compels dismissal of plaintiffs' claims.

D. The Fact That Plaintiffs Have Asserted A Purported Defense That Cannot Be Litigated Does Not Entitle Them To Prevail In This Default Termination Case

Finally, plaintiffs' implicit argument that the Government should be made to "pay" for its invocation of the state secrets privilege is incorrect. In ascertaining the effect of a state secrets privilege assertion, the Government may not be "penalized," but must be treated in the "same" manner as a private party. *E.g.*, *In re United States*, 872 F.2d at

[14] *Petrochem Services, Inc. v. United States*, 837 F.2d 1076 (Fed. Cir. 1988), is not to the contrary, but holds that in those rare cases in which the Government is attempting to rebut an allegation that it failed to transmit "superior knowledge" by showing that it did, in fact, orally convey that knowledge to the contractor, the Government must show that the oral communication was understood. *Petrochem* is, thus, consistent with the innumerable authorities confirming that contractors bear the burden of establishing all elements of an alleged breach of an implied duty to share superior knowledge.

476 ("Notions of sovereign immunity preclude . . . adverse consequence to the government, such as alteration of procedural or substantive rules"), *citing*, *Ellsberg*, 709 F.2d at 65 ("the effect is the same, in other words, as if the government were not involved in the controversy"); *Salisbury v. United States*, 690 F.2d 966, 976 (D.C. Cir. 1982); *Pan American World Airways, Inc. v. Aetna Casualty & Surety Co.*, 368 F. Supp. 1098, 1139 (S.D.N.Y. 1973), *aff'd*, 505 F.2d 989 (2d Cir. 1974); *Sigler V. LeVan*, 485 F. Supp. 185, 192-95 (D. Md. 1980); *Kinoy v. Mitchell*, 67 F.R.D. 1, 15 n. 50 (S.D.N.Y. 1975). *See also* 4 J. Moore & J. Lucas, *Moore's Federal Practice* ¶ 26.61 at 26-257 (1979) (no unfairness where "a suit against the government for breach of contract, permitted only by the grace of the sovereign, fails because the plaintiff is unable to obtain information because of a claim of privilege.").

Moreover, merely because plaintiffs have purported to tie their defense to a non-justiciable, attenuated claim of superior knowledge, they cannot insulate themselves from their failure to perform this A-12 contract. Plaintiffs are not precluded from defending against the default termination claim here -- they are only foreclosed, properly, from pursuing their ancillary claim that the Government breached an implied contractual duty to share secret, classified "superior knowledge." That superior knowledge claim, because it is inextricably intertwined with state secrets, cannot be litigated, and must be dismissed.

CONCLUSION

For the reasons stated above, we respectfully request that the Court dismiss plaintiffs' "superior knowledge" claims.

Respectfully submitted,

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December 23, 1993

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
	)	No. 91-1204C
Plaintiffs,	)	
	)	Filed: February 16, 1994
v.	)	
	)	
UNITED STATES OF AMERICA,	)	
	)	
Defendant.	)	

ORDER

Defendant has rejected the court's request that it meet with plaintiffs and security officers to consider a means of trying any of plaintiffs' superior knowledge claims because those claims are "inextricably intertwined" with privileged matters. However, the cases repeatedly cited by defendant address factual situations far different from this one. For example, in *Zuckerbraun*, a tort action against a private corporation, plaintiff alleged that a weapons system was defective, and the system itself was declared a state secret. Information essential to proving plaintiff's wrongful death claim was privileged.

General McPeak's declaration informed the court that further inquiry regarding certain low-observable technology would pose an unacceptable risk to national security. Plaintiffs assert that only a portion of their superior knowledge claims implicates the low-observable technology described by General McPeak.

The declaration of Albert P. Farr III executed November 18, 1993 asserts that of three areas of superior knowledge, only development of the low-observable suite involves the sensitive technology described by General McPeak. Mr. Farr details other alleged superior knowledge of the United States in areas of weight and manufacturing/materials experience. General McPeak's declaration, which is not an invocation of the state secrets doctrine, does not specifically address those areas.

Defendant's unwillingness to negotiate a means to try any of these claims or to provide a comprehensive invocation of the state secrets doctrine does not permit us to rule for defendant by default. The Government may choose not to cooperate because of legitimate concerns for national secrets, but defendant must show the court why the cost of such a decision should be borne by plaintiffs.

A hearing is set for March 7, at 10 o'clock a.m. in the National Courts Building for defendant to show cause why we should not deem admitted plaintiffs' superior knowledge claims that do not implicate the low-observable technology described by General McPeak.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	Filed: March 7, 1994
Defendant.	)	

DEFENDANT'S MOTION FOR LEAVE TO FILE RESPONSE TO THE COURT'S ORDER TO SHOW CAUSE, AND RESPONSE TO ORDER TO SHOW CAUSE

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DEFENDANT'S MOTION FOR LEAVE TO FILE RESPONSE TO THE COURT'S ORDER TO SHOW CAUSE, AND RESPONSE TO ORDER TO SHOW CAUSE

By order dated February 16, 1994, the Court scheduled a hearing for March 7, 1994, and directed the Government to show cause why the Court should not enter findings against defendant.

So that the position of the United States is stated clearly for the record, we respectfully request leave to file the following written response.

DEFENDANT'S RESPONSE TO THE COURT'S ORDER TO SHOW CAUSE

The Government desires to make several points. First, although the type of discovery negotiation proposed was not appropriate for a variety of reasons, the Government does not wish to foreclose a full investigation of whether any possibility of litigating plaintiffs' "superior knowledge" claims exists, and we therefore set forth below (at pp. 2-3) what we perceive to be a workable framework that would allow further exploration of this question. That framework would be established, in part, under the personal cognizance of the General Counsel of the Navy.

The Government also wishes to emphasize that, at this time, it does not appear that any portion of the "superior knowledge" claim pursued by plaintiffs

is truly separable from information subject to the state secrets privilege.

Finally, in its order dated February 16, 1994, the Court directed the Government to show cause why the Court should not deem admitted some portion of plaintiffs' superior knowledge claims. The reasons why the Court should not deem such claims admitted include: (i) even if some portions of plaintiffs' claims are separable, plaintiffs have not proven the elements of those claims, and no authority supports findings in their favor in these circumstances; and (ii) if there is a "cost" to be borne here, the law provides that it should be borne by plaintiffs.

1. Defendant's Proposed Framework For Determining Whether It Is Possible To Litigate Any Part Of Plaintiffs' "Superior Knowledge" Claims

For the reasons described in part 2 below, the Government's position is that, at this time and on this record, plaintiffs' "superior knowledge" claims must be dismissed. In addition, as explained below, the Government was compelled to decline to engage in the sort of negotiation session initially proposed by the Court, and pursued by plaintiffs.

Upon further reflection and consultation with senior Government officials, however, and in order to remove any doubt regarding the justiciability of plaintiffs' claims, we propose (without prejudice to, or waiver of, our position), the following framework

for exploring whether further litigation of plaintiffs' "superior knowledge" claims is possible.

a. Plaintiffs pose to the Government in writing narrow, particularized, specific questions for discovery, and demonstrate how each such question bears on their superior knowledge claims. (Such questions could not involve LO technology, because, as plaintiffs admit, that information is clearly intertwined with state secrets.) This procedure will enable a determination to be made as to whether the plaintiffs have a need, for the information. The procedure will also prevent plaintiffs from engaging in a fishing expedition in highly classified matters.

b. To avoid wasteful duplication of effort, and undue demands upon the very senior Government officials who would be involved in this process, plaintiffs should be required to submit all of their questions at one time, with no piecemeal submissions.

c. The Government, under the personal cognizance of the General Counsel of the Navy, will take these questions to the officials responsible for knowledge of the subject matters, and also to the responsible security decision makers within the Department of Defense (or elsewhere), and determine, consistent with a good faith effort to declassify and disclose as much information as possible, whether any of these questions could be answered without invading matters classified outside of the A-12 program, for which the state secrets privilege would be asserted. The General

Counsel of the Navy will promptly so advise the parties and the Court, in writing.

d. No deposition discovery would proceed until completion of this process and evaluation of the results, and until further order of the Court. If such depositions eventually occur, strict and enforceable constraints upon the subject matter of the inquiries would be imposed.

If this proposal cannot be adopted, then we do not believe that there is a way around the predicament which arises from the non-justiciable nature of plaintiffs' "superior knowledge" claims. For the reasons described below and in our prior briefs, plaintiffs' claims would have to be dismissed.

At the hearing on February 3, 1994, the Court inquired whether a framework for litigating plaintiffs' claims was possible, and cited the "ejection seat" as a potential area of allegedly-unshared information that might be pursued by plaintiffs as a basis of their superior knowledge claims. *E.g.*, 2/3/94 Tr. at 59. While such a postulated claim might be justiciable (or might not be, as the Court recognized, *see* 2/3/94 Tr. at 59), it does not resemble the actual claims that plaintiffs have stated in their complaint, pursued in discovery, or attempted to pursue after the February 3, 1994 hearing. After that hearing, plaintiffs immediately sought to fully recommence their superior knowledge discovery (terminated by the Court on May 7, 1993, and again on August 11, 1993) into the B-2 and F-117A programs. App. 1. The essence of that discovery concerns allegations

involving the sort of low observable ("LO") information that, as plaintiffs must recognize, will never become a part of this lawsuit. *E.g.*, App. 2-3.

As we understood the negotiating suggestion made by the Court, Government security officers, Government lawyers, and plaintiffs' lawyers would meet to discuss the information needed for litigation of plaintiffs' claims and the Government' s defenses to those claims. Presumably, the security officers would then inform the attorneys that certain areas of inquiry were problematic for security reasons, and negotiate the scope or nature of the information that could and could not be produced and disclosed.

Unfortunately, such a procedure would not be workable, in part, because it would essentially be a mechanism for removing relevant information from the case without a formal invocation of the state secrets privilege. Because of its constitutional significance, removal of relevant evidence from a case because of national security concerns is an undertaking that requires the various formal procedures specified by the Supreme Court in *United States v. Reynolds*, 345 U.S. 1 (1953), and its progeny. The contemplated negotiation, however, would circumvent *Reynolds, et al.*, by potentially removing relevant evidence from the case -- *i.e.*, when a security official identifies it as problematic in a negotiation session -- without the necessary procedural safeguards required by *Reynolds*, and without creating a record for review. In addition, the resultant claims and defenses that would emerge for trial would bear no relation to plaintiffs' real claims,

to the Government's defenses, or to the factual reality upon which the merits of those claims and defenses will depend. That is one of the reasons why the cases require that courts dismiss a claim if that claim, as framed and pursued, is inextricably intertwined with state secrets.

2. There Is No Separate, Justiciable, Non-Privileged Portion Of The "Superior Knowledge" Claims That Plaintiffs Could Pursue In This Action

The procedure described in part 1 above is suggested in a good faith effort to resolve all doubts on the "superior knowledge" issue. For the record, however, we are constrained to state that it remains the Government's position that upon this record plaintiffs' "superior knowledge" claims should be dismissed.

Plaintiffs allege that the Government breached an implied contractual duty to share information contained in "other classified, special access programs related to, among other things, weight estimation techniques, application of low observable technologies, propulsion system technologies, composite materials and composite manufacturing technologies, and avionics technologies (especially those relating to achievement of low observability)." Second Amended Unclassified Complaint !50. In connection with those broad allegations, every time that plaintiffs have had an opportunity to pursue "superior knowledge" discovery, they have requested information relating to sensitive LO areas, ~, App. 1,

2-3, and they have sought to inquire about information contained in other special access, LO weapons programs. Accordingly, litigation of plaintiffs' allegations would "would present a continuing threat of disclosure of information for which the military and state secrets privilege has been asserted, and would present a need for disclosure of additional information over which [the privilege would be asserted]." 7/22/93 McPeak Decl. ¶ 5.[1]

Plaintiffs' pleadings confirm that they have not abandoned the LO portions of their superior knowledge claims.[2] For example, plaintiffs' proposed

[1] It is not merely a theoretical possibility that the discovery plaintiffs seek regarding materials would threaten inadvertent, unauthorized disclosure of privileged information -- that type of discovery has resulted in such disclosures in this case. We respectfully refer the Court to the circumstances surrounding the deposition of Admiral David E. Jeremiah, taken by plaintiffs on July 19, 1993. *See* 11/19/93 Defendant's Response to the Court's Order, Etc., App. at 8-9.

[2] Plaintiffs have, however, abandoned their previously -- asserted argument that detailed and technical information contained in other special access programs need not necessarily have been shared by the Government. *See McDonnell Douglas Corp.& General Dynamics Corp. v. United States*, 27 Fed. Cl. 204, 206(1992) ("a warning may have been sufficient"). Even if plaintiffs could establish the other elements of a superior knowledge claim, the Government did provide a warning to plaintiffs regarding weight estimates. *E.g.*, Cate Decl. ¶ 4,Govt. Ex. 36 to Classified Appendix to Defendant's Statement of Genuine Issues In Response To Plaintiffs' Proposed Findings Of Uncontroverted Fact, dated December 28, 1993 ("GRPPF"); *see also* GRPPF No.7, at pp. 20-21. Faced with that dispositive fact, plaintiffs now argue that such a warning did not contain

findings of uncontroverted fact -- findings that plaintiffs believe the Court must make, in order to rule in their favor -- are dependent upon allegations relating to the LO characteristics of the aircraft they failed to build. *See e.g.*, Plaintiffs' Proposed Findings of Uncontroverted Fact, dated November 22, 1993, No. 3 (general reference to "knowledge from the B-2 and the other classified programs,"); No. 12 (allegation of "superior knowledge with respect to low observables,"); No. 18 (alleged lack of "detailed information regarding the full-scale development of a low observable aircraft,"); No. 22 (alleged unawareness of "signature status or specific technical approaches to signature reduction"). To postulate that a non-classified, non-LO, non-privileged portion of plaintiffs' "superior knowledge" claims exists is to fashion a claim that even plaintiffs do not even assert.

In addition, the November 18, 1993 declaration of Albert P. Farr demonstrates how the purportedly separate areas of "superior knowledge" involve the LO characteristics of the A-12 aircraft, and, therefore, the state secrets privilege. Mr. Farr's position is that the contractors' erroneous weight estimation occurred because the contractors failed to consider the weight implications of "stealth aircraft or other non-conventional configurations," 11/18/93 Farr Decl ¶ 8, and, by his admission, a large portion

"sufficiently detailed technical information." *E.g.*, Plaintiffs' Reply To Defendant's Opposition To Plaintiffs' Motion For Summary Judgment On Count IX, dated January 31, 1994, at 31.

of the "A-12' s overweight condition occurred in the LO suite." *Id.*, ¶ 11. For the parties to litigate superior knowledge "weight" issues (*e.g.*, for the plaintiffs to prove the alleged superior knowledge portion of their weight problems, or for the Government to challenge the allocation and cause of those problems asserted by plaintiffs), the sort of LO information that plaintiffs concede is off limits would be, necessarily, implicated.[3] In other words, the Farr declaration demonstrates how "inextricably intertwined" plaintiffs' claims are with information for which the state secrets privilege has been, and would be, asserted.

In short, while the Court suggests that plaintiffs could amend, or trifurcate, their claims, we believe that the very nature of the claims that plaintiffs allege demonstrate that the claims may not be parsed in such a manner.[4] That, in sum, is the basis for our motion to dismiss.

[3] Unlike then-Acting Secretary of the Air Force McPeak, Mr. Farr is of the opinion that the information that would be disclosed by continued litigation of plaintiffs' superior knowledge claims is not of the sort that "must be protected in the interest of national security." Farr Decl. ¶ 6; *compare* McPeak Decl. ¶¶ 7-8, 10-13. The law does not vest Mr. Farr with authority to make that judgment call, and plaintiffs' efforts to contradict the McPeak and Donley declarations on this point are unavailing.

[4] We have described how such claims cannot be extricated from privileged matters in the following pleadings: (1) 5/27/93 Motion to Dismiss, at 12-22; (2) 7/23/93 Supplement, at 1-4; (3) 11/19/93 Brief In Response To Court's Order, at 20-22; (4) 12/28/93 Opposition To Summary Judgment And Cross Motion, at 13-18; (4) 12/28/93 Statement of Genuine Issues (with classified

* * *

The Court's order to show cause suggested the possibility that it might make findings against the Government at this time. We submit the following brief response.

3. Even If Plaintiffs' "Superior Knowledge" Claims Could Be Segregated, Plaintiffs Have Not Proven Any Portion Of Those Claims, And No Authority Supports Findings Adverse To The Government

In the present posture of this case, there is no authority or rationale that would support the "deemed admission" of any of the allegations that plaintiffs have stated in their complaint, or elsewhere. As the Court correctly held in its published order dated November 1, 1993, litigation of plaintiffs' superior knowledge claims cannot proceed

appendix), passim; and (5) 1/10/94 Reply, at 5-8. We also respectfully refer the Court to the *in camera* materials filed in connection with the assertion of the state secrets privilege and the Government's associated motion to dismiss, including the declaration filed by plaintiffs. Taken together, these materials establish beyond cavil that litigation of plaintiffs' "superior knowledge" claims cannot occur without reference to the privileged information. Indeed, on multiple occasions, this Court itself has noted that the privileged information is "relevant," *e.g.*, 3/18/93 Order; 5/7/93 Order, and that the privileged material is "crucial" to the resolution of plaintiffs' superior knowledge case. *E.g.*, 3/31/93 Order; 4/12/93 Order; 4/14/93 Order.

at present without endangering disclosure of information over which the state secrets privilege has been, and would be, asserted. *McDonnell Douglas Corp. & General Dynamics Corp. v. United States*, 29 Fed. Cl. 791 (1993).

Under this ruling, the Court must decide for one party or the other upon the pending cross-motions that the Court, in part, invited. *Id.*; see also 5/7/93 Order. As we have previously established, the authorities overwhelmingly require the dismissal of plaintiffs' claims. If the Court instead abandons what we believe is its correct prior ruling that litigation of plaintiffs' claims cannot proceed, then the parties would have to recommence "superior knowledge" discovery. We have described in part 1 above the only possible framework which would allow exploration of the possibility of such continued discovery without endangering national security.

4. If There Is A "Cost" To Be Borne In These Circumstances, It Must Be Borne By These Plaintiffs

Finally, in its February 16, 1994 order, the Court stated that the Government must show why the cost of the state secrets assertion, and the consequent non-justiciability of plaintiffs' claims, "must be borne by plaintiffs." 2/16/94 Order.

The assumption that there is a "cost" to be borne in these circumstances logically requires an assessment that plaintiffs could have a meritorious claim on the merits. Plainly, that is what this issue

is all about, and the evidence currently in the record will not support such a finding by the Court. As set forth more fully in Defendant's Statement Of Genuine Issues In Response To Plaintiffs' Proposed Findings Of Uncontroverted Fact, dated December 28, 1993, even the "frozen," non-privileged record10in this case establishes: (i) that plaintiffs received a "general warning" regarding the alleged weight estimation problems they encountered, *id.* at 21-22; (ii) that plaintiffs themselves, rather than the Government, were responsible for any delay or inadequacy of access to B-2 information; and (iii) that plaintiffs had the opportunity for immediate access to any F-117A information that they might have needed. *Id.*, *passim*; *see also* materials cited in Defendant's Opposition To Plaintiffs' Motion For Summary Judgment, dated December 28, 1993, at 5-12.

Moreover, even if there were a "cost" imposed by the circumstances, the plaintiffs here, just like the plaintiffs in *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544 (2d Cir.1991) and *Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1141(5th Cir. 1992), *cert. denied*, 113 S. Ct. 1843 (1993), must bear that cost. The cases overwhelmingly establish that the Government cannot be financially penalized in a lawsuit to which it is a party merely because it asserts the state secrets privilege. *E.g.*, *Ellsberg v. Mitchell*, 709 F.2d 51, 65 (1983) ("the effect is the same, in other words, as if the government were not involved in the controversy"), *cert denied*, 465 U.S. 1038 (1984); *Salisbury v. United States*, 690 F.2d 966, 976 (D.C. Cir. 1982); *Pan American World*

Airways, Inc. v. Aetna Casualty & Surety Co., 368 F. Supp. 1098, 1139 (S.D.N.Y. 1973), *aff'd*, 505 F.2d 989 (2d Cir. 1974); *Sigler v. LeVan*, 485 F. Supp. 185, 192-95 (D. Md. 1980); *Kinoy v. Mitchell*, 67 F.R.D. 1, 15 n.50 (S.D.N.Y. 1975). Simply stated, to grant judgment for private third-party plaintiffs in an effort to shift costs to the Government because of perceived equitable considerations is contrary to the plain holdings of the cases, and would be in error.

CONCLUSION

For the reasons stated above, and in our prior submissions, we respectfully request that the Court dismiss plaintiffs'" superior knowledge" claims. In the alternative, we request that the Court adopt the framework we have proposed above, in order to explore whether any part of plaintiffs' "superior knowledge" claims can be litigated.

Respectfully submitted,

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March 7, 1994

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C
v.	)	Filed: April 28, 1994
UNITED STATES OF AMERICA,	)	
Defendant.	)	

ORDER

Defendant removed certain information from this case by Acting Secretary Donley's invocation of the state secrets privilege. Later, General McPeak advised the court that discovery of plaintiffs' superior knowledge claims as then proposed could be a threat to national security. For that reason, we terminated discovery and directed the parties to address whether a superior knowledge case could proceed.

Since then, plaintiffs have made a reasonable showing that they can proceed without risking national security. They supported that showing with the declaration of an engineer who is in a position to make an informed judgment. Defendant's response

was to point out that this person is not the head of a Government agency, and to insist that we must dismiss plaintiffs' claims because they are inextricably intertwined with privileged information.

Repeated use of the term "inextricably intertwined" does not prove to the court that the assertion is correct. Neither do defendant's citations to its pleadings or to comments from the court. Defendant has not established that plaintiffs' claims are inextricably intertwined with state secrets. General McPeak has not made the showing that Secretary Garrett did in *Zuckerbraun*.

Defendant invites the court to dismiss all superior knowledge issues because of its attorneys' conclusion that plaintiffs' case is inextricably intertwined with state secrets. We are not permitted to do this. We may consider an adequate declaration by the Secretary of the Air Force, for example, and we would accord it due deference.

Defendant includes in its inextricably intertwined theory the concern that its attorneys may be denied access to classified information which may bear upon the Government's defense. We cannot dismiss plaintiffs' claims on the basis of defendant's speculative assertion of prejudice. It is not sufficient for defendant to assert that its litigation team may be unduly hampered by its own security restrictions; it must demonstrate conclusively that continuation of this phase of the case would cause an injustice. Defendant's inability or unwillingness to make the required showing leaves us no choice but to lift the stay of discovery.

We are mindful of General McPeak's admonition, and the court's concerns about security lapses are expressed throughout the record of this case. However, we have access to Air Force, Navy and Justice Department experts who are sophisticated in handling security matters. We have confidence in their ability and integrity, and we have reason to believe that such security lapses will not recur.

Therefore:

1. Plaintiffs' discovery of its superior knowledge counts will proceed at a measured pace, under the close supervision of the court and its security officers.

2. Plaintiffs may review Air Force documents contained in the B-2 and F-117A programs, in concert with the limitations established by Secretary Rice. After that review is complete, plaintiffs will advise the court of any additional discovery needs.

All parties must cooperate with the court security officers, who will inform the court immediately of any problems they may discern. Violations of security procedures would be in contempt of this Order, and we would address such contempt to the full extent of this court's authority.

We have made an effort to justify the Federal Circuit's confidence in the court's ability to "find ways to manage the pace of discovery that do not usurp the [Executive's] power to grant access to classified, compartmented data." If the foregoing

procedures are not effective, we will direct the appropriate agencies to provide the court with information sufficient to litigate this case, pursuant to 28 U.S.C. § 2507 and RCFC 34(d).

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C
v.	)	Filed: December 9, 1994
UNITED STATES OF AMERICA,	)	
Defendant.	)	

ORDER

Plaintiffs allege in Count XVII that they were improperly terminated for default. We held trial beginning September 1993 and agreed to defer substantive rulings to facilitate settlement negotiations. The Navy urged further delay in July, and plaintiffs objected. Additional delay in ruling on Count XVII is not warranted.

Testimony and other evidence at trial showed that the A-12 contract was not terminated because of contractor default. The contract was terminated because the Office of the Secretary of Defense withdrew support and funding from the A-12. Prior

to that, the Navy did not believe that the contractors' performance justified termination for default.

Detailed findings of fact will be submitted following trial on the remaining issues. The decision terminating the contract for default was not properly made and therefore is VACATED.

IT IS SO ORDERED.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

* * * * * * *

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,

Plaintiffs,

v.

UNITED STATES OF AMERICA,

Defendant.

* No. 91-1204C

* Filed: April 7, 1995

* * * * * * *

ORDER

Court security officers completed a review of matters related to litigation of Count IX and issued a thoughtful and thorough report that includes several options for the court to consider. The report contains the following comment: "We have very great security concerns with discovery potentially involving some of the Nation's most sensitive and perishable secrets."

This report was issued nearly a year ago, and we were concerned about such observations from these security professionals, and by similar sentiments expressed by General McPeak. However,

for reasons stated often before, we are not free to dismiss major issues from litigation merely because such risks appear. The law does not permit us to prejudice a party in such a manner, solely because we are unwilling to accept such risks. We may do so only in response to a proper invocation of the state secrets privilege by a qualified official of the United States Government. Although the Justice Department has argued repeatedly that Count IX is inextricably intertwined with state secrets such that it cannot be litigated, the Executive Branch for whatever reason has not been willing to invoke the privilege on that basis.

We issued an Order in April of last year directing the parties to continue discovery on superior knowledge with certain limitations. This discovery has created a number of disputes, but generally it has proceeded without serious incident. We are not aware of further security problems during the past year, and this is a credit not only to the professionalism of our security officers but also to that of the attorneys on both sides. Now, we find that new problems related to plaintiff's allegations of superior knowledge may arise. This may or may not result in more attorneys and more support personnel being exposed to more secrets.

These individuals come and go, and as discovery continues the number of people who know about pieces of the Stealth Program will grow. Even programs with limited access such as the B-2 and F-117 are limited only by the number admitted at any given time -- not by the total number of persons

who pass through. Were it not for this litigation, possibly hundreds of people would not be burdened by knowing some of "the Nation's most sensitive and perishable secrets."

Plaintiffs believe that they can make the necessary showings concerning superior knowledge without reference to most of the evidence that is highly sensitive. We have reason to think that this would be very difficult. In any event, the possibility remains that the case will settle before trial. Another possibility is that defendant will not meet its burden of showing "egregious default" during its case in chief. For these and other reasons, it may never become necessary to litigate Count IX issues. If that happens, the risks that we have run, and continue to incur pre-trial, will have been entirely unnecessary.

Therefore, it is ORDERED:

1. Superior knowledge issues will be litigated separately. That is, we bifurcate Count IX and related Counts, along with issues of quantum, for later proceedings if necessary.

2. The purpose of trial in November is to allow defendant to prove "egregious default." We have discussed applicable standards and burdens in earlier Orders. Once we are in a position to rule on that threshold issue, we will direct further proceedings as appropriate.

3. Superior knowledge discovery is suspended until after we rule on the issues scheduled for trial in November.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

No. 91-1204C
(JUDGE HODGES)

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION AND GENERAL DYNAMICS CORPORATION,

Plaintiffs,

V.

THE UNITED STATES,

Defendant.

DEFENDANT'S RESPONSE TO PLAINTIFFS' STATUS REPORTS CONCERNING SUPERIOR KNOWLEDGE AND THE ORDER OF PROOF AT TRIAL

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IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DEFENDANT'S RESPONSE TO PLAINTIFFS' STATUS REPORTS CONCERNING SUPERIOR KNOWLEDGE DISCOVERY AND THE ORDER OF PROOF AT TRIAL

Defendant respectfully submits this response to Plaintiff McDonnell Douglas Corporation's Memorandum on Superior Knowledge Discovery in Response to the Court's February 7, 1996 Order, dated February 28, 1996 ("MDC's Status Report"), and Plaintiff General Dynamics Corporation's Status Report Regarding Superior Knowledge Discovery and the Order of Proof at Trial, filed February 29, 1996 ("GD's Status Report"). In their separate status reports, the plaintiffs take slightly different approaches to the same result -- namely, suggesting an unnecessarily complicated presentation of the order of proof at trial, requesting an unsupported and unnecessary resumption of discovery into other

classified programs, and contending that, notwithstanding the Court's August discovery deadline and November trial setting, they have no obligation to identify or quantify their Requests for Equitable Adjustments ("REAs") until some future time, if ever. Plaintiffs' suggestions are profoundly misguided and should be rejected.

Instead, as we explain more fully below, plaintiffs' order of proof is flawed in concept, unnecessarily complicated, and would needlessly and unduly prolong the damages phase of this litigation. Plaintiffs can and should fully identify, quantify, and support their REAs by the April 30, 1996 deadline, or abandon them. Complete and timely disclosure is especially critical because, contrary to plaintiffs' mistaken assertions, plaintiffs cannot avoid litigating the merits of their REAs during the forthcoming damages trial. Indeed, it is undisputed that plaintiffs would have lost money on the A-12 FSED contract absent an adjustment to the contract ceiling price. Similarly, because plaintiffs were undeniably in a loss position on the A-12 contract, their argument that the Government should be required to justify the application of a loss adjustment to any termination for convenience recovery is completely unfounded and has the potential to significantly prolong the damages phase of this litigation. Finally, plaintiffs have provided the Court with no basis for the Court to vacate its stay of discovery into other classified programs.

* * * *

IV. Contrary to Plaintiffs' Suggestion, The Factual Record Defeats Rather Than Supports Their Superior Knowledge Allegations

Plaintiff MDC has taken the opportunity, in the guise of attempting to justify plaintiffs' need for superior knowledge discovery, of arguing the purported merits of plaintiffs' superior knowledge case. MDC Status Report at 5-11. Such argument is irrelevant and unnecessary at this point, and normally would require no response. We must respond, however, to avoid any possible inference that we have acquiesced in MDC's factually and legally erroneous description of the allegedly "overpowering factual record" regarding superior knowledge. MDC Status Report at 5.[1]

A. The Navy Did Not Withhold Vital Information From the Contractors

The factual record assembled during discovery convincingly refutes plaintiffs' contentions concerning the existence of superior knowledge. This is not surprising, given that the plaintiffs had a contractual relationship with Lockheed during the concept formulation and demonstration validation phases of the program, and were accessed to both the

[1] The Government opposes MDC's request to take further classified discovery in the B-2 program, and also opposes GD's request to take "unclassified" discovery in the B-2 or any other separately accessed programs. *See* GD Status Report. The Government, of course, does not oppose further discovery concerning superior knowledge from information contained within the A-12 program.

B-2 and F-117 programs early in the performance of the A-12 contract. The plaintiffs found no vital information contained in those programs then, because they judged the F-117 and B-2 technical information to be fairly old technology that would not have changed their course of action on the A-12. The contractors refused the Navy's offer to negotiate a face-to-face exchange of technical information with Northrop in 1988, and failed to continue their relationship with Lockheed into the FSED A-12 contract. In short, plaintiffs made a business decision during contract performance that they did not need the technology available from Northrop and Lockheed. Thus, the only "need" for this information emerged in late 1990, when plaintiffs' lawyers attempted to formulate legal excuses for plaintiffs' failed performance on the contract.

Further, the factual record does not support plaintiffs' contention that "[i]t is now beyond dispute that the A-12 was intended by the most senior officials in the Navy to be a 'miniature' B-2." MDC's Status Report at 6. The factual record assembled to date amply demonstrates that the plaintiffs were very familiar with the design philosophies that had guided the creation of the F-117 and B-2, and that no vital information was withheld from them.

1. In 1988, The Navy Offered the Plaintiffs Face-to-Face Meetings with Northrop's Engineers to Discuss The B-2 Program, But the Plaintiffs Refused To Meet Directly with Northrop

In 1988, plaintiffs were offered face-to-face technical exchanges with Northrop, but refused to meet directly with Northrop. Although plaintiffs now claim that Northrop possessed information essential to their successful performance of the contract, in 1988, when the plaintiffs were offered the opportunity to obtain that information through full and open discussions with Northrop engineers, they declined that opportunity.

At his deposition, MDC's Albert "Pike" Farr acknowledged that he chose not to meet with Northrop engineers in 1988 to discuss the B-2 program. Mr. Farr testified:

> We held conversations between General Dynamics and McAir regarding the advisability of directed discussions with Northrop Corporation. It was my recommendation that we not meet directly with Northrop because of the possibility of proprietary rights infringement, that is Northrop proprietary rights infringement.

Deposition of Pike Farr, Aug. 1, 1995, at 114. App.21-22.

Similarly, GD's Dr. S. Keith Jackson acknowledged that he would have preferred face-to face exchanges with Northrop, but that he had deferred to Pike Farr:

> Well, my preference would probably have been, from a technical standpoint, face to face contacts. I thought that would probably work better. However, Pike had been through that kind of thing before on another previous program and I hadn't. So I essentially deferred to his judgment on that because he had more experience with those sort of exchanges than I had. *From a technical standpoint, a contractor to contractor relationship would have been better.*

Deposition of Dr. Keith Jackson, June 21, 1995, at 89-90 (emphasis added). App. 23-24.

In short, the plaintiffs were given access to the B-2 program, but refused the full and open access offered by the Navy in 1988. In 1990, the plaintiffs did agree to a face-to-face exchange of information with Northrop. When the plaintiffs did gain full access to the Northrop data, they concluded that earlier access to the Northrop data would not have caused them to change their course on the A-12. As Dr. Jackson explained regarding the 1990 exchange of information:

> Q. Do you recall at some point in 1990 indicating in an interview or a meeting that -- and when I say

you, I'm meaning you, Dr. Jackson -- saying that, after reviewing the B-2 data, you concluded that there was not much that you would have done differently, that the B-2 used fairly old technology, and that the technology would not have changed much of what you did on the A-12?

A. I don't specifically remember saying that, although that probably would have reflected my opinion.

Q. So that's consistent with your recollection?

A. Yes.

Q. And do you also recall -- or do you recall having said also in 1990, either in an interview or in a meeting, that with regard to schedule and weight, if you had had a better idea of what the B-2 went through, you would have planned better, but that your technology was better and in fact you beat out the B-2 team for the A-12 contract?

A. I think that's probably also fairly accurate.

Q. So that's consistent with your recollection?

A. Yes.

Id. at 173-174. App. 26.

2. Plaintiffs Had Access To Information Available In The F-117 Program

At the time of contract award, the Navy had no reason to believe that the contractor team lacked access to Lockheed's expertise in stealth technology. In their Best and Final Offer (BAFO), the contractors announced their intention to subcontract with Lockheed on the A-12 contract. Lockheed had worked with the contractors during the concept formulation and demonstration/validation phase of the contract. The contractors stated in their BAFO that they, together with their subcontractor team, had "the total current operational experience" with respect to this type of aircraft. Executive Summary, Volume I, 6 March 1987 at 9. App.27-28.

In 1987, Lockheed, the creator of the F-117, was a leader in the field of stealth technology. The contractors viewed the participation of Lockheed, as well as their other subcontractors, Brunswick and Rockwell, as key to their ability to succeed on the FSED program:

> The Recommended Plan: Issue [a Request for Proposal] (with one suggested exception) that includes all [radar absorbing structure] components (and some specialized [radar absorbing material]) to [Brunswick], [Lockheed]

> and [Rockwell]. (These are the only sources known to be capable and willing to support the [A-12] program.) Each has proven themselves by performing well under Dem/Val subcontracts.

Letter from Frank Kirkland, Engineering Program Manager, to John Lamers, A-12 Program Manager, and Harry Snodgrass, A-12 Deputy Program Manager, dated Aug. 3, 1987. App. 29.

In 1988, the contractors made the business decision to terminate their relationship with Lockheed. The reasons given for terminating the relationship included cost reasons and the relationship's "marginal technical benefit." Letter dated May 12, 1988 from John Lamers to Charles Anderson, Vice President/General Manager, General Dynamics. App. 34. Although the plaintiffs decided to forego a direct contractual relationship with Lockheed, in 1989 the Navy briefed the contractors on the F-117 program. Again, Keith Jackson admitted that access to information from the F-117 program in 1989 probably would not have affected the contractors' course of action on the A-12:

> . . . Our evaluation of the F-117 after we had had a chance to look at it was that it was enough different than the A-12 and enough behind the A-12 that it probably would not have been tremendously useful to us at that stage. It may have been useful a few years earlier, but at that stage it was

> probably overcome by the newer technology.

Deposition of Dr. Keith Jackson, June 21, 1995, at 167. App. 25.

Besides Lockheed, Brunswick, and Rockwell, the contractors subcontracted with General Electric Company, which had provided the engines for both the B-2 and F-117 programs. The team assembled by the contractors for the A-12 thus possessed access to the expertise that had created the engines, inlets, and exhausts for the B-2 and F -117, as well as the expertise resident at Lockheed, Brunswick, and Rockwell.

3. The A-12 Was Not Intended to be a "Miniature B-2"

Contrary to plaintiff MDC's contentions (*see* MDC Status Report at 6), most senior officials did not intend for the A-12 to be simply a "miniature" B-2. Neither the Navy nor the Office of the Secretary of Defense ("OSD") had that intention. Instead, the intention was that the A-12 use stealth technology to perform its medium attack mission. As Dr. David S.C. Chu testified:

> My point is that no one in OSD was saying that the answer for what became the A-12 had to be a miniature B-2. To the extent that was the enthusiasm, it was the enthusiasm, in my judgment, that came out of Secretary Lehman, not out of OSD. OSD emphasis was on a new technological base for this mission,

and -- which included, given the thought process of the time, signature reduction.

Deposition of Dr. David S.C. Chu, Aug. 9, 1993, at 21. App. 35-36.

Similarly, the director of the Navy's Low Observable Office, Admiral William Miller testified at his deposition that the A-12 was not intended to be a miniature B-2. The A-12's design was consistent with the accepted design philosophies of the time. Admiral Miller noted that he had seen a B-2-like design produced by General Dynamics even before he had seen Northrop's B-2:

> Q. Secretary of the Navy Lehman testified last week that part of the acquisition strategy with respect to the ATA aircraft was that it was supposed to be a mini B-2. Are you familiar with that concept?
>
> A. I wouldn't describe the A-12 in exactly that way. I would say it had many of the design philosophies of the B-2 that were accepted design philosophies in industry at that time, *but I don't believe it was designed to be a shrunken version of the B-2.*
>
> In fact, the first time I saw a -- the first time I recollect seeing anything that looked like the B-2 was actually from General

> Dynamics. It looked B-2 like, but it wasn't from Northrop. It was more consistent with the design philosophies at that time.

Deposition of William C. Miller, Aug. 4, 1995, at 90-91 (emphasis added). App. 37-38.

Margaret Claire Schumacher, a NAVAIR engineer with responsibility for radar cross section specification development, testified at her deposition:

> Q. Did you believe at the time that you were developing the spec that the aircraft that would be the A-12 was supposed to be a mini B-2?
>
> A. No.
>
> Q. Did you ever hear anybody in discussions express that belief?
>
> A. No.
>
> Q. You don't recall any?
>
> A. No.
>
> Q. Looking back today, do you think it was supposed to be a mini B-2?
>
> A. No.

Deposition of Claire Schumacher, July 20, 1995, at 115-116. App. 39-40.

Therefore, MDC's contention that the A-12 was intended to be a "miniature B-2" is contradicted by the record.

B. Northrop's Proposal Did Not Contain Superior Knowledge That Should Have Been Disclosed to the Contractors Before Contract Award

Plaintiffs cannot seriously contend that the Navy was obliged to reveal to them the technical details of Northrop's proposal in order to point out perceived weaknesses in the plaintiffs' approach. The law precludes a procuring agency from identifying technical weaknesses if doing so would put an offeror in a better competitive position than it would otherwise have enjoyed. *See, e.g., Saco Defense System Division v. Weinberger*, 806 F.2d 308, 312-13 (1st Cir. 1986); *Ford Aerospace and Communications Corp.*, 80-2 CPD ¶ 439 at 22 (1980). The agency must inform a competitor of any failures to meet the specification, not of all technical flaws discovered in a proposal. No mandate exists to reveal each and every imperfection in a proposal. Above all, the FAR prohibits technical leveling or technical transfusion by sharing with one competitor technical information contained in another's proposal. 48 C.F.R. § 15.601.

Further, there was nothing in the Northrop proposal that should have warned the Navy that the A-12 would be harder to build or more expensive than the contractors realized. John Dorsett, a supervisor charged with developing cost estimates for weapons systems within the Naval Air Systems Command, reviewed both the Northrop and the contractors' proposals prior to contract award. Mr. Dorsett testified:

> . . . What I'm really saying here is Northrop did nothing in the estimating to lead you to believe that they thought the plane was going to be harder to build or more expensive than McDonnell Douglas/GD. In fact, just the opposite was true.

Deposition of John Dorsett, Aug. 22, 1995, at 103. App. 41-42.

Northrop proposed a design that was different from the contractors' design. The Northrop design would have weighed more and had a different radar cross section than the design the contractors proposed and tested as a pole model during the demonstration validation phase of the program. Problems that Northrop perceived in connection with its own design are not applicable to the contractors' design, and there was no reason for the Navy to communicate these problems to the contractors.

What is significant is that the contractors' engineers saw no difficulty with their own design's meeting the A-12 specification requirements. The GD engineer in charge of the signature proposal for the contractors, Glen Arey, testified at his deposition that he believed that his design would achieve the contract's signature requirements:

> Q. Were you satisfied with this final specification -- that is, the January 1988 specification -- as being attainable and achievable?

A. Yes, and we did achieve it on the pole model.

Q. Were there any aspects of your experience following January 1988 through contract termination that caused you to believe the specifications were not attainable?

A. No.

Deposition of Glen Arey, Sept. 7, 1995, at 18. App. 43-44.

In sum, the Northrop proposal documents do not reveal vital information from the B-2 program that was known to the Navy and was brought to the Navy's attention prior to contract award.

CONCLUSION

For the foregoing reasons, plaintiffs should be required to identify and fully quantify their REAs, and not defer this discovery to some unspecified future time. The Court should reject plaintiffs' proposed order of proof as fundamentally flawed, unwieldy, and likely unduly to protract the damages phase of this case. Finally, there is no need to permit discovery in other classified programs, as any evidence of superior knowledge should be evident from A-12 program discovery, and plaintiffs' claim of an "overpowering factual record" supporting their superior knowledge contentions is legally erroneous and is squarely contradicted by the facts of record.

Respectfully submitted,

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you were [15] read into the B-2 program in September or October 1988. Is [16] that correct?
[17] A: Yes.
[18] Q: Okay. Was there someone from the Navy who [19] facilitated your being read into the B-2 program?
[20] A: As I recall Jeff Cook spearheaded the effort [21] to get the initial contacts made with the Air Force.
[22] Q: Okay. Do you recall in that timeframe that [23] you were read in any discussions between yourself, Jeff
[24] Cook, and Dr. Jackson, Keith Jackson, regarding the means by [25] which information would be exchanged between the A-12

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[1] program, GD/McAir, and the B-2 program?
[2] A: Yes.
[3] Q: What do you recall about those conversations?
[4] A: We held conversations between General [5] Dynamics and McAir regarding the advisability of directed [6] discussions with Northrop Corporation. It was my [7] recommendation that we not meet directly with Northrop [8] because of the possibility of proprietary rights [9] infringement, that is Northrop propriety rights [10]infringement.
[11] It was my suggestion that –
[12] Q: Could I just stop you there, please? When [13] you say possibility of proprietary rights infringement, [14] Northrop proprietary rights

infringement, are you saying [15] that you were concerned that proprietary rights held by [16] Northrop could be infringed?
[17] A: That's right.
[18] Q: Okay. Please go ahead then.
[19] A: That we would inadvertently perhaps utilize [20] information that Northrop considered proprietary and [21] subsequently get involved in a lawsuit. I had been involved [22] in the lawsuit between McDonnell Douglas and Northrop on the [23] F-18 and had spent quite a bit of time working on that [24] particular lawsuit and was very sensitive to the possibility [25] of getting into inadvertent litigation as a result of

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[1] inadvertent proprietary information usage.
[2] Q: Okay. In this area, I want to be clear up [3] front, and I will caution you with or before your counsel [4] does. I am not asking for privileged communications between [5] you and counsel, okay, and I do not mean to, and I want to [6] make sure my question does not elicit that, okay?
[7] A: (Witness nodded indicating an affirmative [8] response.)
[9] Q: But, please, if you could explain for me what [10] you meant when you said that you had spent quite a bit of [11] time working on that lawsuit between McDonnell Douglas and [12] Northrop? How did you spend quite a bit of time working on [13] that lawsuit?
[14] A: I participated in the document research for [15] the lawsuit. I participated in some of the write-

ups that [16] were done that were utilized for the lawsuit.
[17] Q: Were these factual write-ups?
[18] A: I don't recall now.
[19] Q: Okay.
[20] A: And I was deposed twice as part of that [21] lawsuit.
[22] Q: Okay. What was the outcome of that lawsuit?
[23] A: The lawsuit was finally settled. I don't [24] remember the date, but it was finally settled between [25] Northrop and McDonnell Douglas out of court.

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[1] Q: Okay. You stated that there were [2] conversations held between McDonnell Douglas and General [3] Dynamics regarding the advisability of direct communications [4] with Northrop. Do you recall stating that?
[5] A: Yes.
[6] Q: Who participated in those discussions between [7] McDonnell Douglas and General Dynamics?
[8] A: Myself, Harry Snodgrass, John Lamers, Keith [9] Jackson. Those are the names that I can recall.
[10] Q: Can you recall anyone else being present in [11] these discussions who you just cannot remember their –
[12] A: There may have been others that I don't [13] recall.
[14] Q: Of the three other gentlemen you mentioned, [15] do you recall any others who shared your concern regarding [16] inadvertent litigation?

[17] A: Yes. Mr. Snodgrass was also concerned about [18] the potential for litigation.
[19] Q: Okay. Do you recall whether Dr. Jackson [20] favored direct communications with Northrop or instead using [21] the Navy and Air Force as conduits of the information?
[22] A: I don't recall that Keith had a position. He [23] may have; I just don't recall.
[24] Q: Do you recall if Captain Cook had a [25] preference as to how the information would be exchanged

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[1] between the contractors on the A-12 and Northrop?
[2] A: I don't recall that he had a preference.
[3] Q: Okay. You mentioned that there were [4] discussions between yourself, Mr. Snodgrass, Mr. Lamers, and [5] Dr. Jackson. Do you recall how many discussions you had on [6] this issue?
[7] A: No.
[8] Q: Okay.
[9] A: More than one.
[10] Q: Okay. At any of those discussions do you [11] recall counsel for either McDonnell Douglas or GD being [12] present?
[13] A: I just don't recall who was – who else was [14] involved.
[15] Q: Okay. On the F-18 program, do you recall if [16] there was a proprietary agreement between Northrop and [17] McDonnell Douglas?
[18] A: I don't recall.

[19] Q: Had you ever been involved in any other [20] programs that caused you concern regarding the inadvertent [21] disclosure of proprietary data other than the F-18?
[22] A: I had been involved in other programs that [23] required use of proprietary data, yes.
[24] Q: Did a problem arise regarding the inadvertent [25] release of proprietary information?

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[1] A: On the other program?
[2] Q: Yes.
[3] A: No.
[4] (Farr Deposition Exhibit No. 120 [5] was marked for identification.)
[6] BY MR. KIRSCHMAN:
[7] Q: Mr. Farr, I am going to ask you to please [8] review what the court reporter has marked as Deposition [9] Exhibit No. 120.
[10] A: I've reviewed the document.
[11] Q: Okay. Do you recall, Mr. Farr seeing this [12] document, the draft agreement and the cover slip, any time [13] prior to today?
[14] A: No.
[15] Q: In this timeframe, August 15th of 1988, were [16] you aware of the existence of a draft proprietary data [17] agreement?
[18] A: No.
[19] Q: Looking at the first page of the exhibit, [20] page 144, do you know who Pat Hogan is?
[21] A: Yes.

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Probably contracts department. Pat Hogan worked on the program. I'm sure James Mifsud did also.

Q. When you say "worked on the program," do you know in what capacity they worked on the program?

A. Well, Pat was kind of our contracts guy. He sort of led our area there.

Q. And is it your understanding he reported to Mr. Wright or someone else?

A. I'm not sure what his reporting chain was. Probably to Mr. Wright, I suspect.

Q. And do you recall what any of his particular responsibilities were?

A. No. You'd really need to try to talk to Mr. Wright to get the details. He was the one that dealt with a lot of our contractual agreements. I think he was probably a lawyer.

We'd tend to go to him with legal questions at times also.

Q. Did he work with subcontract issues, as you recall?

A. He was really not in the procurement department. But again, for a complete description of his duties I'm not the right

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one to ask on that.

Q. And how about Mr. Mifsud?
A. Again, you need to talk to him or some of the people in his chain. Robert Wright would be a better person to talk to about his
Q. Do you recall whether he was an attorney?
A. I think so, but I am not sure. I think so.
Q. Any recollection whether he was in the general counsel's office or Mr. Wright's shop?
A. I don't know. It could have been both. Mr. Wright was a program person and the general counsel's office was a functional department.
So there was a project it was a project organization, a cross-functional organization.
Q. Do you ever recall having any discussions with either Mr. Mifsud or Mr. Hogan about a proprietary data agreement involving Northrop?
A. I don't recall at this date having

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those conversations, although I may very well have. I simply don't recall them.
Q. This document's dated August 15, 1988. Does that or the document at all refresh your recollection?
A. Well, we were, Pike Farr and I, were formally briefed into the B-2 program. We

had
tried to get proprietary agreement exchanges between the B-2 and the A-12 in 1988. We were
briefed into the B-2 program from a security standpoint in Washington, in Crystal City. I think that was probably the latter part of
1988, and I suspect that this was right before that.
We came up and had a briefing in one of the Air Force offices in the Pentagon, primarily a security briefing. But they showed us
a . .
picture of the B-2 and just a very top-level description of the airplane by an Air Force officer in what's now the Air Force AQL office.
And then after that we later had another briefing by John Griffin and one of the other engineers on the B-2 in Dayton about

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B-2 characteristics. We spent, as I remember, a day or so up there. I remember Captain Cook
was also with us.
Then Captain Cook briefed the Air Force people on the A-12. I suspect that was probably in 1989 some time.
Q. Do you recall there being any hesitancy on the part of anyone in MCAIR in 1988 to sign a proprietary data agreement

such
as this one?
A. I don't specifically remember it. I know that Pike Farr was somewhat hesitant to talk directly to Northrop and I think he had some concerns about some of the ongoing ATF competitions and getting into legal problems because of the very complex relationship, being teamed on one program and competitors on another one.
Q. Do you recall in the 1988 time frame any discussions between yourself and Jeff Cook and Pike Farr involving the methodology or the process for technology exchange with Northrop?
A. Yes. As I recall, and again my memory is fuzzy, but as I recall we did want to exchange information between the programs.

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I remember Pike was concerned about direct contractor to contractor exchanges because of some of the legal issues associated with the other competitions that were going on, and I remember he was in favor of having exchanges between the Government people on the B-2 and the A-12 with the contractors.

(8) In other words, his recommendation
(9) was that the Government brief, the Government
(10) A-12 people learn about the B-2 and then brief
(11) the contractor A-12 people, but with the
(12) proviso that they could screen proprietary
(13) information that could be a legal problem.
(14) And then the same thing would happen with
(15) information that's transmitted to Northrop
(16) from A-12, so that it was a Government to
(17) contractor relationship.
(18) But he was concerned that the contractor
(19) to
(20) contractor relationship could
(21) cause legal problems.
(22) Q. Was that the same approach that you
(23) had at that time?
(24) A. Well, as far as "you" do you mean
(25) General Dynamics or my approach?

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(1) Q. You Dr. Jackson, did you prefer face
(2) to face?
(3) A. Well, my preference would probably
(4) have been, from a technical standpoint, face
(5) to face contacts. I thought that would
(6) probably work better. However, Pike had been
(7) through that kind of think before on another
(8) previous program and I hadn't. So I
(9) essentially deferred to his judgment on that
(10) because he had more experience with those sort
(11) of exchanges than I had.

From a technical standpoint, a contractor to contractor relationship would have been better.
Q. Do you recall what Jeff Cook's preference was?
A. I don't recall that right now.
Q. Do you recall Jeff Cook advocating face to face contact between the contractors?
A. I honestly don't recall what his position was.
Q. Do you recall some time ago you prepared a declaration or an affidavit for some pleadings in this litigation dealing with the exchange of technology?

* * * *

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Force representatives there?
A. Yes, there were Air Force representatives who did the briefing. As a matter of fact, there were no Lockheed people there that I know of. It was totally Air Force.
Q. You don't recall anyone from Lockheed being present at the briefing?
A. That's correct.
Q. Do you recall which Air Force individuals were present?
A. No, I don't recall the specific Air Force individuals who were there.
Q. Do you recall the Navy individuals?
A. I don't recall them, either. I suspect that there were people from the program office and I suspect that Jeff Cook

may have been there, but I can't specifically remember him being there.
Q. Do you recall about how long the meeting went?
A. Oh, I suspect that we probably had a half day, something like that.
Q. Was it your recollection that you had the opportunity to forward your selected

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questions out there in advance?
A. It was my recollection that we did not, for some reason. I think we basically had to carry them out in our head, but I can't swear to that.
Q. Do you recall whether there was some kind of briefing before you started asking your questions?
A. We had only a very minimal briefing, and the main the main subject of the meeting really came down to looking at the airplane and talking about supportability issues, maintainability, operational issues. The Air Force people there really knew very little about the technical capabilities of the airplane.
Q. When you say looking at airplane, that's the F-117, not the A-12?
A. That's the F-117.
Q. Do you recall whether there were any subsequent meetings with Lockheed?
A. There were not.
Q. Do you recall why that was?
A. I don't recall why that was. Those

(25) simply never got organized. We were all
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(1) debriefed from the F-117 program after the
(2) meeting and told to erase our memory banks.
(3) Q. Do you recall whether this briefing
(4) was similar to the B-2 briefing in that there
(5) was some quid pro quo?
(6) A. No, this briefing was, if you compare
(7) it to the B-2 briefing in early 1990, the F-111
(8) briefing was had far less technical content
to
(9) it.
(10) We did have a chance to talk
(11) to Air Force maintenance people and
operators,
(12) so it had more hands-on maintenance kinds of
(13) things. But relatively light on the technical
(14) content of the airplane.
(15) Q. When you say "operators," do you mean
(16) pilots?
(17) A. Pilots and ground crew, crew chiefs,
(18) maintenance people, the list of people that
(19) worked on the airplanes, and some of the
(20) pilots also.
(21) Q. Do you recall undertaking any efforts
(22) later in the A-12 FSD program to obtain
(23) information referring to the 117?
(24) A. We verbally asked for information
(25) referring certain certain technical subjects.
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(1) We asked to have information transmitted to
us
(2) on the F-117 after we knew about that, as well

as the B-2 and other classified programs that we felt were out there, but we did not have a name on. So in terms of trying to get specific, get F-117 information, I don't remember a specific F-117 information request that went out similar to what we had on the B-2. As I mentioned, we were asked not to mention that we had been there and be debriefed from the program. So our requests had to be quite general when we came back.

Q. Do you recall ever pursuing a quid pro quo technology exchange with Lockheed for 117 information?

A. No. No, this was between, as I remember, between us and the Air Force,

Q. And do you recall why you never made the offer to have one of those type of exchanges with Lockheed?

A. Well, I think we expressed our willingness to do that. It simply never got off the ground, for some reason. The request

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had to go through the services.

Q. So so far as you know, that issue was never raised directly with Lockheed?

A. I don't know whether it was or not. I simply don't know.

Q. Do you recall raising the issue with

Jeff Cook, of a quid pro quo technology type exchange with Lockheed?
A. I don't specifically remember raising the issue in that term, a quid pro quo exchange.
Our evaluation of the F-117 after we had had a chance to look at it was that it was enough different than the A-12 and enough behind the A-12 that it probably would not have been tremendously useful to us at that stage. It may have been useful a few years earlier, but at that stage it was probably overcome by the newer technology.
Q. So when you say the F-117 was behind, you mean behind technologically?
A. Technologically.
Q. So your belief was that by 1989 the A-12 was more advanced technologically?
A. Yes, significantly.
Q. And do you recall ever having a

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discussion with Jeff Cook to the extent of, why don't you go see if Lockheed wants to know anything from our program, maybe there's something we can exchange, get some information from them?
A. I don't remember discussing anything in that particular term, in those particular terms. We may have, but I don't recall that kind of a conversation. Our conversations tended to

be more that, we need information on any problem areas we had from other classified programs that we don't know about. We never got down to trying to, as I remember, to offer particular trades of information on F-117.

Q. When you say the F-117 was behind the A-12, was that in terms of structure or avionics or everything?

A. More or less everything. And they also had different approaches than we had. Their approach to things was different. Just simply because it was different, the things that they were doing were not directly applicable to where we were at that time. If

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we had had some of the F-117 information earlier in the program, it may have helped some.

By 1989, as far along as we were in the program, we didn't see a whole lot that we thought would be of great benefit. At least, as I said, we didn't get an in-depth technical briefing, but from what we saw it did not look like there was a great deal of information that we could have employed at that time in terms of impacting the airplane.

There was some interesting information on maintenance problems and operational issues that would have been

valuable later, later on in that phase of the program.
Q. But your impression was that by the summer of 1989 when you saw the F-117 that Lockheed had nothing to offer you that was going to help you get to first flight or help you get to FSD?
A. Right. I wouldn't say absolutely nothing. That's very all-inclusive. But almost nothing.

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Q. Do you ever recall Lockheed approaching you to have any kind of technology exchange, saying, we hear you have some technology, is there anything we can offer you?
A. I don't remember that specifically, although I do remember vaguely that we did talk to some of the Lockheed people at one occasion on some of the hot exhaust materials and that we did have some exchanges on that. And I'm not sure when that was. Some time during the program. That's the only thing specific I remember about that.
Q. Do you recall if that was F-117 related?
A. I did not know enough about what the F-117 had to know. The materials that we were using were Space Shuttle tile-derived materials.
Q. Is that like the tile that Rockwell was

A. I think Lockheed probably supplied the tile for the Space Shuttle to Rockwell, and we were using materials derived from that. The Skunk Works may have used that same kind of material on F-117, but we were not

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knowledgeable enough to know where that was. We had people – nobody was briefed on F-117 except for that very brief period that a few of us went out there. So for most of the time, we had very little idea what was available on the F-117 or not available. We couldn't talk about it if it were.

Q. And it's your recollection that when you were talking to Lockheed about the thermal barrier tile – is that the correct term?

A. Yes, it's the thermal barrier tile.

Q. And is that for, for example, the pitch flap region?

A. This would be used for the pitch flap, possibly the [ ] possibly some of the regions of the fixed trailing edge.

Q. And is it consistent with your recollection that that was in the same line of materials that Rockwell was using on the Space Shuttle, that Lockheed provided to Rockwell?

A. It was my impression that the materials were derived from those same kind

of
(24) materials. They may not have been identical,
(25) but it was that line of technology that
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(1) developed that kind of material.
(2) Q. Do you recall that Rockwell used
(3) reasonably small pieces of tile in, for
(4) example, a mosaic formation, and you were
(5) looking for much larger pieces?
(6) A. We were looking for larger pieces and
(7) shaped pieces, although ours did not
(8) necessarily have to be very large. We could
have
(9) put
(10) strain isolation layers and so forth
(11) on it. But it was certainly not identical
(12) probably to the Space Shuttle tiles.
(13) Q. Do you recall having discussions with
(14) Lockheed later about materials other than
that
(15) thermal tile?
(16) A. I don't recall any. There may very
(17) well have been some, but I would not have
been
(18) involved in those discussions personally.
(19) Q. Is it your recollection that you
(20) expected that you may have gotten more
useful
(21) information from the B-2 program?
(22) A. Yes.
(23) Q. Is it your recollection that the B-2
(24) technology was also older than the A-12
(25) technology?

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A. In some respects it was, in some respects it wasn't. The A-12 I think had better signatures in general than the B-2 had. There were different approaches taken in different places, and the B-2 was a much larger airplane. A lot of the B-2 information that would have been most valuable to the A-12 was not signature information, however.

Q. Do you recall at some point in 1990 indicating in an interview or a meeting that – and when I say you, I'm meaning you, Dr. Jackson – saying that, after reviewing the B-2 data, you concluded that there was not much that you would have done differently, that the B-2 used fairly old technology, and that the technology would not have changed much of what you did on the A-12?

A. I don't specifically remember saying that, although that probably would have reflected my opinion.

Q. So that's consistent with your recollection?

A. Yes.

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Q. And do you also recall – or do you recall having said also in 1990, either in an

interview or in a meeting, that with regard to schedule and weight, if you had had a better idea of what the B-2 went through, you would have planned better, but that your technology was better and in fact you beat out the B-2 team for the A-12 contract?

A. I think that's probably also fairly accurate.

Q. So that's consistent with your recollection?

A. Yes.

MR. SCHOONER: Can we go off the record for one moment.

(Discussion off the record.)

(Jackson Exhibit No. X-74 was marked for identification.)

BY MR. SCHOONER:

Q. The Court Reporter is handing you what he's marked as Exhibit 74. Do you recall ever having seen this document before?

A. I don't recall having seen this particular one before.

840

[REDACTED]

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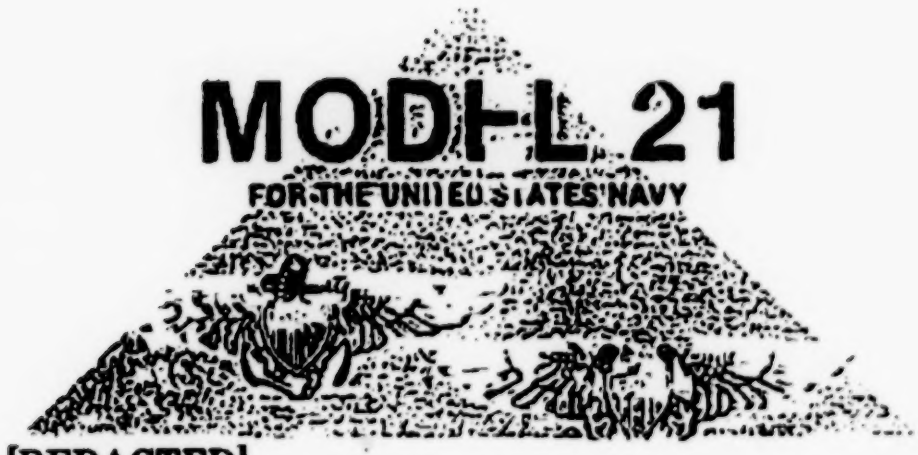
6 March 1987



[REDACTED]

I Executive Summary
Volume 1 Executive Summary (U)

[REDACTED]

[illegible] | GENERAL DYNAMICS
[illegible]ONNELL AIRCRAFT COMPANY | Fort Worth Division

This proposal or quotation includes data that shall not be disclosed outside the Government and shall not be duplicated, used, or disclosed in whole or in part for any purpose other than to evaluate this proposal or quotation. If, however, a contract is awarded to this offeror or quoter as a result of or in connection with — the

submission of this data, the Government shall have the right to duplicate, use, or disclose the data to the extent provided in the resulting contract. This restriction does not limit the Government's right to use information contained in this data if it is obtained from another source without restriction. The data subject to this restriction are contained herein.

[REDACTED]

I EXECUTIVE SUMMARY
Volume 1

(U) Electromagnetic Emissions Are Controlled

[REDACTED] Intentional and unintentional EM emissions are managed to enhance survivability. Low-probability-of-Intercept (LPI) modes of operation (spatial, power, and frequency manipulation) are employed. RF emissions are minimized through highly integrated emission management techniques, emphasizing passive operation of systems and sensors in all mission phases.

[REDACTED] *Multi-Company* **[REDACTED]** *Are Employed*

[REDACTED] MCAIR and GDFW are industry leaders in developing and applying signature reduction technologies to operational tactical aircraft. Some notable examples are the Radar Target Scattering Facility, RATSCAT, which

was designed, built and operated by GD; F-111, the first operational aircraft using Radar-Absorbing Material (RAM) and Radar-Absorbing Structure (RAS) and meeting an RCS Spec; Gray Butte, site of much [REDACTED] testing built and operated by MCAIR: Tomahawk and Advanced Cruise Missile, using LO [REDACTED] technologies: [REDACTED]

[REDACTED] In order to assure the best [REDACTED] experience available, particularly in the area of RCS, the MCAIR/GDFW team has utilized Lockheed and Rockwell International as subcontractors during the Dem/Val phase. This combined team has the total current operational experience on [REDACTED] aircraft. The final selection of [REDACTED] and components will be made from the four contractors' proposals, based upon both cost and performance benefits.

[REDACTED] Figure 1-6 shows Model 21 undergoing a portion of the 1000-plus hours of testing that have improved and validated its RCS characteristics. Figure 1-7 summarizes the multi-company, real world experience that reduces Model 21's operational RCS risk.

Figure 1-6 (u) Validated RCS Characteristics

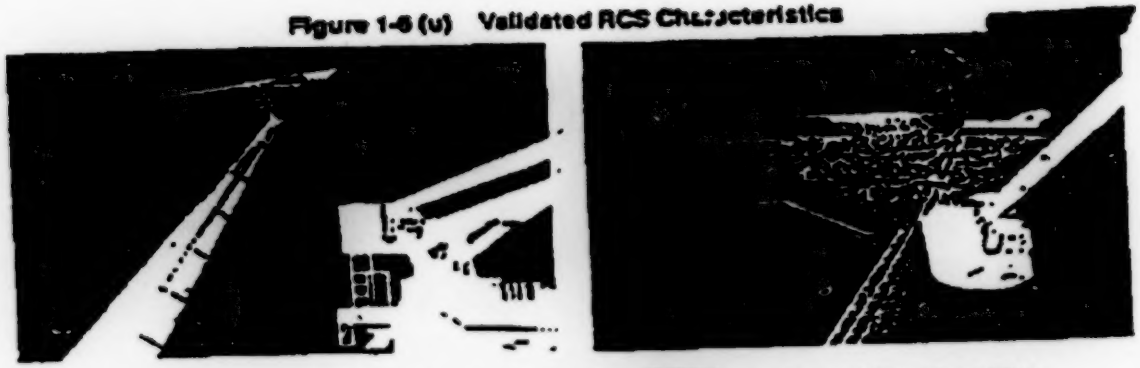
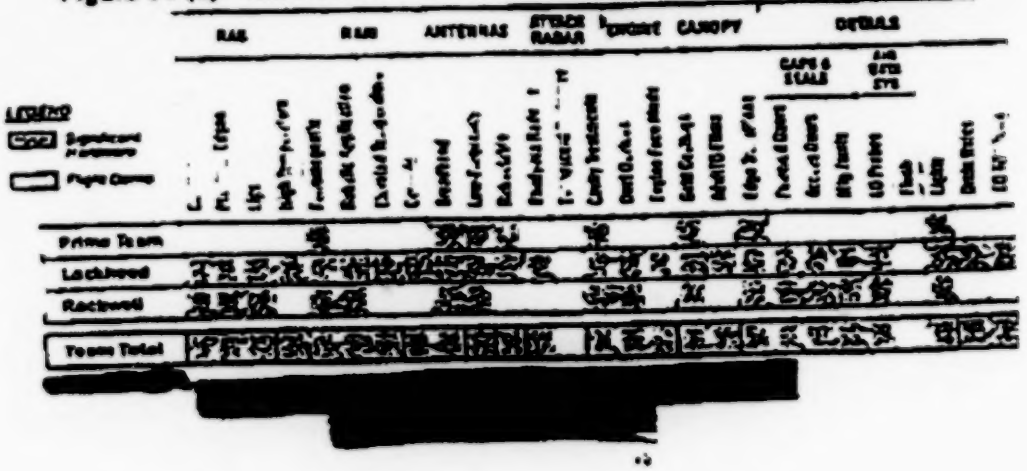


Figure 1-7 (u) Team and Subcontractor [redacted] Experience Minimizes Risk



UNCLASSIFIED
EMS-87-018

3 August 1987

Memo to: J. P. Lamers/H. E. Snodgrass

From: F. P. Kirkland

Subject: Program Radar Absorbing Structure (RAS) Acquisition Strategy

Based upon what I understand to be our program objectives for FSD and our silimar Corporate objectives in this important technical area, a RAS acquisition strategy is recommended which emphasizes fabrication by outside vendors early in FSD but then transitions to a competitive environment in which either 206 or 208 is a source for each RAS component as the production program matures.

This plan is based upon achieving the following four objectives:

1. PROGRAM SUCCESS. Delivery of aircraft on schedule, within cost and which meet stringent performance requirements.
2. LONG TERM TECHNOLOGY OBJECTIVES. To develop the total capability to design, integrate, fabricate, test, and support RAS hardware by both 206 and 208.
3. FAIRNESS. Meet moral, implied, and (in the case of 494) written commitments to provide production

opportunities to our DEM/VAL RAS suppliers.

4. COMPETITION. Customer goal to ultimately have two competing sources for each significant component.

I. The Recommended Plan

1. Issue an RFP (with one suggested exception) that includes all RAS components (and some specialized RAM) to 430, 494, and 899. (These are the only sources known to be capable and willing to support the 206/208 program. Each has proven themselves by performing well under DEM/VAL subcontracts.) Each could then choose to bid on any or all components.

2. Select preferred outside sources for each RAS component by considering risk, performance, cost, and schedule. It is assumed: (a) from what has been seen technically to date, and (b) to minimize overall risk, that each would likely provide, initially, one or more components.

3. It would be a condition of the RFP and subcontracts that each initial outside source bring on as a second source either 206 or 208 (pairings to be based soley upon negotiations between 206 and 208) as a second source on a predetermined schedule and provide all rights, technical data, and tooling, as specified.

4. This phase-in of 206 and 208 as second sources would be similar to the way 206 and 208 become fully competititive aircraft sources by Lot 5. It is suggested that the vendor provide all ship sets

for FSD, Pilot Production, Lot 2, and approximately 70% of Lot 3 (206 or 208 providing the remainder of Lot 3). Full competition (with a source percentage limit similar to that used for other procured two-source items) would begin with Lot 4. (This is one Lot earlier than the time when 206/208 would reach full competitive status but would assure each vendor of building over 40 ship sets plus those won competitively in Lots 4 and beyond.)

5. The competition for Lots 4 and beyond would include provision for technology improvements by 206/208 (or the outside source) to influence the split.

6. The agreements would be limited to aircraft for the initial customer, (i.e., standard "make or buy" decisions at our option would apply to future customers).

II. The Rationale

The primary goal is to provide quality parts on schedule, within cost and with warranty. To do this will require sufficient experience personnel, specialized test and production facilities, and keen determination. There is no doubt that both 206 and 208 have the latter, however, the aggressive FSD schedule being proposed requires more personnel and resources in the RAS area then I believe we presently possess. This viewpoint is highly influenced by our work on RAS for the full-scale model. The sensitivity of the performance to minor design and fabrication variations is alarming. A sufficient number of engineers having the

understanding and skills to do the job are unfortunately not yet available.

Use of outside sources will further reduce the overall risk by assuring that other program risk areas can be better addressed. The vendors would take the initial risks (though we will obviously still share that risk) and 206/208 would come on board when the systems are mature. Just as it will take many engineers to oversee the radar vendors, it will, I believe, consume all our personnel in this technology to determine the requirements, do the system integration, support 206/208 testing, and monitor the performance of the vendors — let alone do all the development, design, and manufacturing.

Initial use of the outside vendors will also make much-needed resources (such as RCS ranges, anechoic chambers, and large autoclaves) accessible. These people and facilities will leverage our own.

The F-16 radome is procured not because we are unable to make it, but because a specialty vendor (430) is better able to accomplish the task. RAS, however, because it is such an integral part of advanced combat aircraft, must eventually become a routine discipline and product of our Corporations. Therein is the motivation that we phase ourselves in as producers it meets our long-term objectives.

Each of these vendors has contributed significantly to our competitive position, especially for the full-scale "test-off" model. I seriously doubt that we would be as competitive now if we had tried to do it by ourselves. They have worked countless long hours and adhered to tight schedules, yet

repeatedly delivered and installed quality components. They have also cooperated with each other and 206/208 amazingly well, liberally providing test equipment, sub-components, and expert advice. They expect, and deserve, a fair shot at the resultant business.

Such a plan should be especially attractive to the competition-minded customer and fulfill their requirements for dual sources. It can be featured as an attractive strength in our BAFO proposal and will contrast with our competitor's reported unwillingness to share their technology with even their own partners.

(The one RAS area recommended for exemption from this plan is the nozzle. I believe a different approach is needed and will offer suggestions in a separate memorandum.)

III. Conclusion

Because of the aggressive schedule of the FSD Program and the limited hardware experience and facilities of 206 and 208, it is strongly recommended that those interested and supportive outside sources be utilized initially. However, because of our corporate goals we then must develop this capability organically. The acquisition plan recommended significantly reduces risk, makes us more competitive, and deals fairly with these vendors, yet achieves our internal objectives. An initial "make" instead of "buy" approach, while quite naturally appealing to many of our functional departments, could seriously jeopardize a successful FSD program.

(And even with these outside resources, it will be a serious challenge!)

/s/ Mark R. Sivers

for

F. P. Kirkland
Engineering Program Manager

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INTEROFFICE MEMORANDUM

Date: 12-May-1988
04:43pm CDT
From: John P. Lamers – FW
LAMERS,JP

Dept:

TO: Charles A. Anderson – FW (ANDERSON,CA)

Subject: Lockheed Termination

Today I directed my people to discontinue their efforts to forge a satisfactory arrangement with Lockheed.

Reasons are as follows:

- Marginal technical benefit
- 14 major terms/conditions issues of which three are show stoppers
- Out of bed $20M on cost
- Inability to achieve a satisfactory security posture.

No appreciable progress has been made in recent weeks on the foregoing items. Our backs are to the

wall on schedule. Accordingly, we must move ahead with alternate plans.

I have a call in to Brizendine to inform him.

John P. Lamers

[1] extent there was an enthusiasm for B-2 being a [2] model, that as much as anything came out of [3] Mr. Lehman. [4] Q: I'm sorry. What was that last [5] sentence again?

[6] A: My point is that no one in OSD [7] was saying that the answer for what became A-12 had [8] to be a miniature B-2. To the extent that that was [9] the enthusiasm, it was the enthusiasm, in my [10] judgment, that came out of Secretary Lehman, not [11] out of OSD. OSD emphasis was on a new [12] technological base for this mission, and – which [13] included, given the thought process of the time, [14] signature reduction. In fact, I think all that [15] Mr. Thayer's memo really says in this – quoting [16] from it – "I strongly recommend that the Navy [17] immediately begin development of an advanced [18] all-weather attack aircraft. Its IOC should be no [19] later than fiscal year 1995, which is a reasonable [20] deadline if the Navy begins its work promptly. The [21] new aircraft should incorporate the technology [22] available by this deadline, but emerging avionics [23] technology should be incorporated, when warranted, [24] on a product-improvement basis. This strategy [25] precludes delaying the aircraft IOC because of a

[1] lack of technological development in avionics [2] equipment."

[3] Q: And was it your understanding, [4] from that language which is in Secretary Thayer's [5] January 11, 1984 memorandum that appears in your –
[6] A: Well, it may be slightly [7] earlier. That – oh, maybe – I guess that's the [8] date they're using for that. That says, "DEPSEC [9] has seen." I'm sorry. Yes. Please.
[10] Q: All right. Was it your [11] understanding from that language that the aircraft [12] would incorporate the air-frame technologies from [13] advanced signature reduction aircraft such as the [14] B-2?
[15] A: I wouldn't want to put it quite [16] that way. I think the presumption I would make, [17] given the structure of the department's thinking at [18] that time, is that signature reduction would be one [19] of the areas that you would incorporate in this [20] program, but that did not necessarily mean using [21] the B-2 solution. The B-2 is, after all, one [22] solution to how to reduce signatures.
[23] Q: The other solution you've [24] mentioned is the first generation F-117 solution?
[25] A: F-117, and we now have, as you

[1] know, a third generation of solutions, which were [2] the two prototype aircraft delivered for the – [3] what – the ATF competition.
[4] Q: But those would not have been [5] available to the Navy in January, 1984.
[6] A: No. But ATF's beginning is [7] roughly at the same time, and so that if people [8] wanted to start with a fresh sheet of paper and [9] say, "Okay, the

goal is I want to carry ordnance [10] this far, I want it to deal with enemies of this [11] sort, I have the following problems to solve, how [12] might I do this," it's quite conceivable people [13] would have come up with a different generation [14] answer. They did not have to emulate B-2 [15] specifically.
[16] Q: But –
[17] A: I don't believe anyone told [18] them to emulate B-2 specifically. I could be wrong [19] about that, but that's not my recollection.
[20] Q: Wasn't the whole point not to [21] start with a fresh sheet of paper, but rather, as [22] we've read before, to use the technologies [23] developed by other programs?
[24] A: No. As I said, my view of that [25] language, although I admit it doesn't say it quite

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[1] this way, is much closer to the spirit of Secretary [2] Thayer's memorandum which preceded it and [3] subsequent debates in the defense resources board [4] in which specifically Secretary Lehman very much [5] agreed with the presumption of Secretary Thayer [6] that it would be unwise to mortgage the IOC of this [7] aircraft and its cost to development of a separate [8] set of avionics for the airplane.
[9] Now, what Mr. Thayer, in [10] my judgment, attempts to do with this memorandum is [11] to have it both ways. "Okay, we're going to put [12] some kind of cutoff on this. We're going to say, [13] you know, technology – we're not going to keep [14] chasing technology forever. Technology as of [15] such-and-such will be used, or to be consistent [16]

with this IOC, but let's not do it stupidly. In [17] other words, structure the avionics so that as the [18] avionics world advances, you can incorporate some [19] of those benefits into your airplane."
[20] Q: Secretary Thayer's language is [21] limited to avionics, as you've indicated in that [22] paragraph that you've read from in his January 11, [23] 1984 memo.
[24] A: Uh-huh.
[25] Q: But the language that I have

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[1] read from Secretary Lehman's memorandum is not [2] limited to avionics, is it?
[3] A: Well, I don't think I want to [4] say that Secretary Lehman – Secretary Thayer's [5] language is limited to avionics. He says, back to [6] this paragraph, "The new aircraft should [7] incorporate the technology available by this [8] deadline, but emerging avionics technology should [9] be incorporated, when warranted, on a [10] product-improvement basis."
[11] He – as I read this [12] sentence, the intent is not to let "better" be the [13] enemy of "good enough," on one hand, but on the [14] other, to signal that in the avionics area, leave [15] provision, as best judgment dictates, for future [16] incorporation of new technological developments.[17] Because as you know, in avionics, we can take boxes [18] out and put boxes in, if we have designed the [19] aircraft thoughtfully to begin with. If you've not [20] left enough space or air conditioning, stuff like [21] that, or you've got a structure which requires you [22] rip

the whole thing out in order to change one [23] aspect of the avionics system, then you've put [24] yourself in a corner. And that's all I see him [25] doing. But, there's nothing in here that says, "You

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[1] have to do B-2.
[2] Q: All right. And you don't [3] recall anything from the discussions at the time [4] indicating that from an airframe point of view, the [5] B-2 signature reduction technologies were what were [6] being contemplated by Secretary Lehman?
[7] A: No. As I said, I would like to [8] turn – I don't have them here, obviously. I'd [9] like to turn to my notes of this presentation to [10] Mr. Taft, but I was struck in that presentation [11] that Mr. Lehman had a specific aircraft in mind as [12] his model, and it was either F-117 or B-2, and your [13] citing of the public document suggests that it was [14] B-2 that Mr. Lehman was enthused about.
[15] Q: Okay. Dr. Chu, I think we [16] have, in our prior session, discussed the A-12 [17] DAB. Do you recall when the DAB was held for the [18] A-12 program, the final DAB before cancellation?
[19] A: You mean December, 1990?
[20] Q: Yes, sir. Do you remember when [21] in December?
[22] A: Yes, sir. I believe that the [23] dates were December 7th and 11th.
[24] Q: And did you receive a briefing [25] from your staff in advance, a pre-brief, for that

along, and at the time the ATF was developed, it was representative of a different capability in industry.

Q: (U) Okay. To be very precise. about it, and for clarity of the record, on page 115 of Exhibit 1, the person actually setting forth the F-22 as third generation was Admiral Kelso in written response to Congressman Dellums' questions. And that's just for clarification of the record sir.

(U) Now, sir, we have identified as three generations of the application of stealth technology, the prehistoric beast was the SR-71, the F-117 was the first generation, and the B-2 was the second generation and the F-22 was the third generation, would you agree with that?

A: (U) Those are rough characterizations and represent design philosophies. Those aren't hard lines, but it's roughly right.

Q: (U) Where in your mind was the ATA aircraft supposed to fit in that

progression?
A: (U) I would say that it would have been – considering the time that it came.

into being, it would be roughly representative of the capabilities in industry circa late '80s. And therefore I'd say I would be surprised if it looked like a 117. I would have thought that it would have looked – been consistent with the design philosophies represented in the B-2 but not unique to the B-2 at that time.
Q: (U) Would you consider the ATA to have been intended to be a generational step?
A: (U) No. Not in the sense of stealth technology.
Q: (U) That's precisely what I meant. Stealth technology is what we're talking about.
A: (U) Yes.
Q: (U) And I'll repeat it just so it's clear for the record and you don't feel in any way compelled here. With respect to stealth technology, it was not your understanding that the ATA was intended to be a generational step beyond the B-2, correct?
A: (U) That's correct.
Q: (U) How would you characterize

what the A-12 was supposed to be vis-a-vis stealth technology and this generational

structure that we just talked about?

A: (U) Consistent with the state of the art.

Q: (U) And what was representative of the state of the art in 1987?

A: (U) Do you mean in terms of manned aircraft in production or in design at that time?

Q: (U) Yes, sir.

A: (U) I believe in 1987 the B-2 was the aircraft – to the best of my recollection, in 1987 the B-2 was the only aircraft in development and production in stealth aircraft.

Q: (U) Secretary of the Navy Lehman testified last week that part of the acquisition strategy with respect to the ATA aircraft was that it was supposed to be a mini B-2. Are you familiar with that concept?

Q: (U) I wouldn't describe the A-12 in exactly that way. I would say it had many of the design philosophies of the B-2 that were accepted design philosophies in industry at that time, but I don't believe that it was designed to be a shrunken version of the B-2.

(U) In fact, the first time I saw

a – the first time I recollect seeing anything that looked like the B-2 was actually from General Dynamics in something that they were pushing early on. It looked B-2 like, but it wasn't from Northrop. It was more consistent with the design philosophies at that time.

Q: (U) Let me ask you this, sir: Recalling what the ATA specification was, ranging from a [REDACT] [REDACT] [REDACT], that the requirement was that it would be all aspect and that the elevation would be [REDACT], what type of platforms are candidates to satisfy such an RCS specification besides a tailless flying wing?

A: (U) I think, to the best of my recollection – and it's been some time since I've addressed these questions, but to the best of my recollection a tailless flying wing was selected as the planform for the A-12 as a result of the competitive design studies that looked at a number of possible planforms and designs that would have certain advantages and disadvantages. Signature being one of them. And that the

planform for the A-12 came from those design

studies and one of the reasons one would go to a
tailless flying wing is signature.
Q: (U) Do you know if the
contractors ruled out the other designs because
they didn't satisfy the RCS specifications?
A (U) I don't recall why a
particular planform was ruled out.
Q: (U) Do you recall that both
Northrop/Grumman/Vought as one team and GD and
McAir as another teamed proposed tailless flying
wings for the final candidates to the ATA
aircraft?
A: (U) To the best of my
recollection, both candidates proposed that.
Q: (U) Do you recall why they
proposed that?
A: (U) No.
Q: (U) Why each team proposed that?
A: (U) Both teams were going through
a trade study – an extensive trade study and
looked at a lot of different applications and a
lot of different potential designs for the
vehicles, because as I said, signature was only
one part of the specification or the operational
requirement for that vehicle and what one might

do for a signature might impede on a contractor's ability to deliver another. So they were trying to trade off, and both started with a very wide spectrum of candidates and eventually got down to only a few.

Q: (U) Wouldn't you agree that the essence of the A-12 aircraft was stealth, sir?

A: (U) No. I'd agree that the essence of the A-12 aircraft was developing - was delivering weapons on target and surviving the experience. Signature control was only one means of surviving that. Speed was another. Altitude, maneuverability, there is a number of ways that one survives the experience of delivering weapons on target. But it was essentially a weapons system, not just how to design an aircraft and to get the signature as low as possible.

Q: (U) Well, you've given a number of factors for consideration to be sure, and those would be reflected in the operational requirement and specification, would they not?

A: (U) They normally are. I don't recall the particular OR.

Q: (U) Let's put it in these terms:

interested in relaxing them, but I'm not positive.

Q: (U) Do any reasons come to mind?

A: (U) You know I'm really not sure that was his stand. I don't remember clearly enough.

Q: (U) And I know it's been a long time. I'm not meaning to press you on things you completely don't remember.

(U) It says here under that same asterisk that "Contractor input is accepted." Was that a prospective thought, do you think, or was that more of a present, the contractor's input has been accepted. Do you follow my distinction?

A: (U) Oh, yes. I think it -- I took it to mean that here's a version of this, and we'll be taking your inputs to it.

Q: (U) I see. So you read this to mean that with respect to the signature levels that the first two bands at the top, that contractor input has been accepted, at this stage I'm talking about?

(24) A: (U) No, I took it to mean that we
(25) would take comments on it.

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(1) Q: (U) So it was prospective?
(2) A: (U) As it was pretty much all the
(3) time through the development.
(4) Q: (U) You'll also notice at the
(5) bottom next to the higher frequency bands there
(6) is what looks like 212 comments with a [REDACT]
(7) next to it. From that and the other reference to
(8) 212 above, does that tell you whether at this
(9) point you were accepting numbers recommended by
(10) Northrop?
(11) A: (U) That's what it – well, it
(12) looks like we were getting their comments in.
(13) Jotting down notes about what their inputs were.
(14) Q: (U) Can you tell from your notes
(15) here what exactly Northrop's input was?
(16) A: (U) Well, it looked like they
(17) made a comment on the second number and a comment
(18) about antenna levels.
(19) Q: (U) Do you remember anything
(20) specific about those comments?
(21) A: (U) No.
(22) Q: (U) Do you recall whether at the

top on the second band whether their input related to the [REDACT] or the [REDACT] that was put into the spec, or what their input was with

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respect to those numbers?

A: (U) I don't remember. I could give a best recollection of what I thought now.

Q: (U) And what would that be?

A: (U) They were thinking those kinds of numbers were achievable.

(U) MR. HELLER: Why don't we break for lunch. This is a good stopping point.

(Noon recess taken.) (U)

(Mr. Reggets is now present.) (U)

(U) MR. HELLER: Back on the record.

Q. (U) (By Mr. Heller) I believe you testified earlier that generally your team was trying to accomplish some of the same things that were done on the B-2, do you remember that testimony, just generally?

A: (U) I said it was a similar kind of requirement.

Q: (U) Did you believe at the time that you were developing the spec that the aircraft that would be the A-12 was

supposed to
(24) be a mini B-2?
(25) A: (U) No.

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(1) Q: (U) Did you ever hear anybody in
(2) discussions express that belief?
(3) A: (U) No.
(4) Q: (U) You don't recall any?
(5) A: (U) No.
(6) Q: (U) Looking back today, do you
(7) think it was supposed to be a mini B-2?
(8) A: (U) No.
(9) (U) MR. HELLER: I'm handing
(10) the court reporter what will be marked as Exhibit
(11) X5 which is a top secret document identified by
(12) number 201/0022-86, and it's a November 7, 1986
(13) version of Appendix F and I'd ask you to just
(14) quickly familiarize yourself with that. Again, I
(15) won't be asking you about most of the specifics
(16) in there.
(17) (Whereupon, Schumacher Deposition (U)
(18) Exhibit Number X5 was marked for
(19) identification by the reporter.)
(20) Q: (U) (By Mr. Heller) Have you had
(21) a chance just to look through it quickly?
(22) A: (U) Yes.

Q: (U) And do you recognize the document?

A: (U) Yes.

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Q: (U) And does this just represent another iteration in the spec development process?

A: (U) Yes.

Q: (U) If you turn to page 3. You should have that RCS basic minimum chart before you and if you could open up to Exhibit X4, to that same chart, that was on page 7 of 11 in the September '86 spec.

(U) You'll notice that on the September '86 spec it looks like that for the [REDACT], it was suggested that the signature level be [REDACT], or at least those are the numbers typed into the document, and then in the exhibit before you, which is the November spec, the signature level for that same range is [REDACT], do you see that?

A: (U) Yes.

Q: (U) Do you recall why the level was relaxed to a [REDACT]?

A: (U) No.

Q: (U) Did you have any involvement

in determining what that signature level should be for that band?

A: (U) It was another iteration.

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Again, this is refinement of the numbers.

Q: (U) Do you know whether you participated in the discussion to relax the spec to [REDACT]?

A: (U) Yes.

Q: (U) But you don't recall the reasons why it was relaxed to [REDACT]?

A: (U) No

Q: (U) Do you consider that a significant jump from [REDACT]?

A: (U) Yes.

Q: (U) And why is that?

A: (U) It's a significant relaxation.

Q: (U) Do you recall any conversations with OPNAV about relaxing the spec to [REDACT]?

A: (U) Not specifically. I think we're still driving at the same questions. This was iteration after iteration of getting data and information. That's about all I can say about any of these questions.

Q: (U) I understand. You had said

that you consider this a significant relaxation,

so I'm just curious exactly what was the

Q: (U) The difference in then-year dollars between the two proposals was approximately $7.8 billion; correct?

A: (U) For FSED.

Q: (U) For FSED.

A: (U) For 1, 2, and 3.

Q: (U) Right.

A: (U) Given, of course, they didn't propose Lot 3.

Q: (U) Right.

A: (U) Yes.

Q: (U) Did that fact concern you when you were doing your estimate?

A: (U) No. Let me explain why. If you looked at the details of the Northrop proposal, and let's just take the three big areas that make up FSED for a second; the design engineer hours, the test and evaluation, and the manufacturing.

(U) The McDonnell Douglas/GD estimate was very significantly higher than the Northrop estimate in each of these areas. You go

back 22 percent higher for the design engineering hours and the text and evaluation. The manufacturing was about 10 percent higher in the McDonnell Douglas/GD estimate.

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(U) What I'm really saying here is Northrop did nothing in the estimating to lead you to believe that they thought the plane was going to be harder to build or more expensive than McDonnell Douglas/GD. In fact, just the opposite was true. A lot of the difference in full scale development is made up by two things: The 580 million we talked about earlier, plus a difference in inflation rates that amounts to about 6 percent. If you take that out, or if you compare the prices of the two airplanes, they're actually very close.

(U) Now, there is another large difference in the numbers in the production lots. None of this is in the actual calculation of the cost or price of the plane. All of this is

driven
(16) by a ceiling factor, a price to ceiling factor o
(17) about 75 percent that Northrop added at the end.
(18) (U) So what I'm really telling you
(19) is that Northrop showed us nothing in a proposal to
(20) allow us to believe that based on any B-2 or other
(21) experience that this plane would cost more than
(22) what GD/McAir thought. All Northrop did was add on
(23) a very high factor at the end of everything.
(24) (U) And the general feeling since
(25) they did it this way, as opposed to showing us

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(1) anything in the estimate that would lead you to
(2) believe that it was higher, our general feeling was
(3) that they simply thought they had the program won
(4) and were trying to make as much profit as they
(5) possibly could get on it. And in fact, we
(6) increased the Northrop estimate in certain areas
(7) where we lowered the McAir/GD estimate.
(8) Q: (U) Do you recall what areas those
(9) were?

A: (U) The design engineering hours section, the system test and evaluation section.

(U) Now, had they done anything in any of the estimating areas, showed us that it should have been a lot higher we would have been very concerned. Had they used a rationale in any of these factors that they added – this 75 percent factor that they added at the end that indicated this was because of their concern, then we, again, would have been concerned.

(U) This was simply something that they stuck in there. So, yes, we looked very close to see if there was a problem because of it. But that was not the way they had done it.

Q: (U) Didn't the fact that they had basically submitted a technical proposal that was

unresponsive and bid less aircraft for more money generate that sort of concern with the cost group?

A: (U) It generated more of a concern that they weren't taking things seriously

and that
it looked like they were trying to almost rip off
the government more so than anything else.
(U) Had they legitimately
presented anything that backed this up, then it
would have been a totally different concern on the
government's part.
(U) And I think what you have to
remember on top of this is that what we were
estimating was significantly higher than anything
in our database, even a supersonic swing wing
F-14. We were well higher than that by 28 percent
manufacturing; by 25 percent design engineering
hours. So we were doing our best to cover this and
had we seen – by cover this, I mean cover this new
technology, and had Northrop showed us anything
that was definitive or specific, we would certainly
have jumped at that, but they did not.
Q: (U) Do you know whether or not
Northrop was asked to show you something

definitive
(24) after the review of their initial proposal?
(25) A: (U) I think they were, but I was

(1) not there. Nothing came down. I know all the
(2) aspects of it were questioned and nothing came down
(3) through the people that had been there, to me, that
(4) Northrop responded in any way as to why these
(5) things should be that way. And believe, me, we were
(6) certainly looking for anything like that because
(7) this was new technology.
(8) Q: (U) The historical database that
(9) you used to do this estimating work, did that
(10) database contain only Navy aircraft?
(11) A: (U) No. The F-15 I already
(12) mentioned and the F-16 are Air Force aircraft.
(13) Q: (U) Do you recall that there was a
(14) $4.2 billion cap on the FSED program at this time?
(15) A: (U) No one ever mentioned anything
(16) to me about a cap. If there was one I was never
(17) aware of it as such. And we did not estimate

toward anything – you know toward any kind of a cap. We estimated it as we understood it.

(U) I think one other comment on the Northrop thing is our estimate and Northrop's, apart from these couple of factors, were quite close.

A: (U) Does that show up in any of your charts in the cost presentation to SSAC?

Aside from the fact that the estimates were quite close. For example –

A: (U) It doesn't for the production lots because we didn't put the detail in here.

Q: (U) Just for the FSD?

A: (U) For the FSED. And that's another point to be raised. They did not have that very high 75 percent factor in FSED, so if this was a real problem, why not put it in. But if you compare our FSED you will see that we are fairly close to Northrop in our estimate.

Q: (U) You said this 75 percent factor, are you talking about the share ratio?

A: (U) No. On top of the price and the production lots, they had a factor to go to ceiling of around 75 percent and that's what made those numbers so high and contributed to that $7 billion difference you pointed out.

Q: (U) Is it a fair interpretation that Northrop added that because of risks they perceived in the FSD part of the program?

A: (U) They certainly didn't state it that way.

Q: (U) How was it stated?

A: (U) They really didn't state

Q. As you became more involved in the A-12 program, was there any individual in the government that you primarily had contacts with?
A. Yes.
Q. And who were they?
A. Herb Heffner and Ken Foulke.
Q. Did you or Charlie Liang attempt to get the LO specification changed or modified in any manner prior to the award of the FSED contract?
A. There were discussions, primarily in the VHF/UHF area.
Q. What do you recall about those discussions?
A. Well, Charlie didn't want to use material for the low frequency. It's [ ] material, and it's basically – well, it's on the order of [ ]. And he didn't want to use it. He didn't like it from the standpoint of it's soft. It is not metal. In other words, you can damage it on a carrier, and he just wasn't a believer in it. He thought we ought to build a metal

airplane and coat it with a parasitic, with a RAM coating, is what Charlie wanted to do.
Q. Did you agree with that approach, building a metal airplane and coating with RAM coating?
A. I was for whatever the Navy wanted. We ended up with a compromise. We did incorporate the [ ] material for a partial VHF/UHF reduction. But it wasn't our primary – what the ATF spec ended up was basically reducing it [ ].
So we didn't want to pay the penalty, the penalty for carrying all of that parasitic material. That isn't what that implies. It's complete perimeter treatment of the planform, and we didn't want to do that, primarily because we – well, from a operational standpoint you have better field of view for your antennas if they're on a leading edge, and so we retained the leading edge.
Q. When you spoke of a compromise between what the Navy wanted and what Charlie Liang preferred, was the result of this compromise the

final LO specification?
A. The compromise was the final. Now, what the Navy wanted, I'm not sure what the Navy wanted to start with. I don't remember them wanting the full VHF/UHF treatment. They may have, but I don't remember. That was before I came on board. What we ended up with was a compromise from what Charlie Liang wanted. We did incorporate VHF/UHF treatment.
Q. That was probably my assumption. I had said you had wanted whatever the Navy wanted.
A. Yes.
Q. I assumed you knew what they wanted.
A. No.
Q. But you did not?
A. No.
Q. After the termination of the A-12 contract, were you involved with a report to the Air Force that was made on the ATA program – that is, the Air Force version of the A-12?
A. Yes.
Did you present a written report or verbal

briefing to the Air Force?

A. Yes, several.
Q. I'm going to show you a Level IV document and ask you if you recognize that as one of the briefings or reports you presented.
(Arey Exhibit No. XX-14 was marked for identification.)
(Pause.)
BY MS. MAIZEL:
Q. Do you recognize this particular report?
A. No. I didn't do this. This was before I came on the AX program. I came on in January of '92. But I agree with the chart on page 29. That is my recollection.
Q. That the document, page 29 of 64, that talks about the basic specification evolution comports with how you remember events transpiring?
A. Yes.
Q. The following page also depicts in graph form the story of the basic specification evolution, and it shows the first draft

of the specification as of August 1986 in graph form, and the final specification, January 1988, also in graph form.

Do these graphs also comport with your recollection of the specification evolution?
A. Yes.
Q. The final specification in January 1988 depicts what is called evolved VHF/UHF.
What do you understand to be "evolved VHF/UHF?"
A. That's some VHF/UHF treatment, but not total perimeter coverage, for the reasons
we stated before.
Q. And that is also reflected in some relaxation of the specification over the VHF and UHF frequencies?
A. Yes. And also it goes on. It looks like it actually goes up to the O and S bands.
Q. And that is depicted by the sloping portion of the graph?
A. Right.
Q. And then at [ ] it levels out.

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at [ ] dBsm?
A. Right. The slope line is the way it really happens naturally is the word I want to say because I don't know of any other right now. That is just the way that the vehicle performs versus frequency.
Q. Were you satisfied with this final specification – that is, the January 1988 specification – as being attainable and

achievable?
A. Yes. And we did achieve it on the pole model.
Q. Were there any aspects of your experience following January 1988 through the time of contract termination that caused you to believe the speicifications were not attainable?
A. No.
Q. I would like to turn to page 35 of 64, the page entitled Low Observable Features. Page 35 of 64 lists the RCS design features. Are these the RCS design features of the A-12 based on the contractor's experience that are listed?
MR. GRAHAM: Objection, vague.

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

Filed March 31, 1998

No. 91-1204 C

MCDONNELL DOUGLAS CORPORATION AND GENERAL DYNAMICS CORPORATION,

JUDGMENT

v.

THE UNITED STATES

Pursuant to the court's published Opinion, filed March 30, 1998, vacating the opinion and order of February 20, 1998, and the corresponding judgment entered February 23, 1998,

IT IS ORDERED AND ADJUDGED this date, pursuant to Rule 58, that plaintiffs recover of and from the United States the sum of $1,200,132,820.00, plus statutory interest from June 26, 1991, until paid. No costs.

David A. Lampen
Clerk of Court

March 31, 1998 By: */s/*

Deputy Clerk

NOTE: AS to appeal, 60 days from this date, see RCFC 72, re number of copies and listing of *all plaintiffs*. Filing fee is $105.00.

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS
CORPORATION AND GENERAL
DYNAMICS CORPORATION

No. 91-1204C

vs.

THE UNITED STATES

At the Court of Federal Claims held in the City of Washington, on the 31st day of March A.D. 1998, judgment was entered as follows: that plaintiffs recover of and from the United States the sum of $1,200,132,820.00, plus statutory interest from June 26, 1991, until paid. No costs.

[For the purposes of 41 U.S.C. § 612(c), the applicable agency is the Department of the Navy; Contract No. N00019-88-C-0050]

A true copy of record.

In testimony whereof I have hereunto set my hand and affixed the seal of said Court of Washington, this 31st day of March A.D. 1998.

/s/ David A. Lampen
David A. Lampen, Clerk

Attest:

/s/ Loren A. Smith
Loren A. Smith, Chief Judge

Nos. 09-1298 & 09-1302

Supreme Court, U.S.
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IN THE
Supreme Court of the United States

GENERAL DYNAMICS CORPORATION,
Petitioner.

v.

UNITED STATES OF AMERICA,
Respondent.

THE BOEING COMPANY,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

On Writ Of Certiorari To The
United States Court Of Appeals
For The Federal Circuit

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BRIEF FOR DEFENDANT-APPELLANT
UNITED STATES

IN THE UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

NO. 98-5096, -5122, 5123

MCDONNELL DOUGLAS CORPORATION,

Plaintiff-Cross Appellant,

and

GENERAL DYNAMICS CORPORATION,

Plaintiff-Cross Appellant,

v.

UNITED STATES

Defendant-Appellant

APPEAL FROM THE UNITED STATES COURT OF
FEDERAL CLAIMS IN 91-CV-1204,
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II. THE TRIAL COURT ERRED IN PRECLUDING THE APPLICATION OF A LOSS RATIO TO PLAINTIFFS' DAMAGES

The trial court's ruling on damages, like its decision to convert the termination for default to a termination for convenience, rests on clear legal error.

A contractor whose contract has been terminated for the government's convenience is entitled to be compensated fairly for the work he has done, "including a reasonable allowance for profit." 48 C.F.R. § 49.201(a). However, "if it appears that the contractor would have incurred a loss had the entire contract been completed," the contractor's claims for profit are ignored, 48 C.F.R. § 49.203(a), and its recoverable costs are reduced "by the ratio of (i) the total contract price to (ii) the total cost incurred before termination plus the estimated cost to complete the entire contract." 48 C.F.R. § 49.203(b)(3). *See also* 48 C.F.R. § 52.249-2 (same).

Thus, even assuming that the termination of the A-12 contract were to be converted to a termination for convenience, plaintiffs' recovery must properly reflect their estimated losses. And it is undisputed – indeed it was the centerpiece of the contractors' claim for restructure and Pub. L. No. 85-804 relief – that had the A-12 contractors ever completed the contract, their costs would have exceeded the contract ceiling price by an enormous amount. Indeed, in their proposal for restructure,

the contractors would have agreed to assume a $1.5 billion fixed loss of the cost overrun. J.A. 18,217.

The trial court, however, declined to calculate plaintiffs' damages in accordance with settled law and with reference to the realities of the contractors' projected losses. The court concluded that if it was impossible to try the Count IX "superior knowledge" claims without endangering state secrets, it should award the contractors their incurred costs and ignore their expected losses. 37 Fed. Cl. at 285, J.A. 227. This ruling is utterly misconceived, for two independent reasons.

First, plaintiffs' superior knowledge claim fails as a matter of law and cannot properly be a basis for refusing to apply a loss ratio. The government has no implied contractual duty to disclose classified information to its contractors – much less the highly classified information contained in the special access programs at issue in this case – except on terms and conditions that it sets in its sole discretion.

Nor can plaintiffs' claim be saved by the trial court's belief that the government might have a duty to provide a "general warning" regarding potential problems with the production of the aircraft. 37 Fed. Cl. at 275 n.7, J.A. 217. The trial court at no time explained what "general warning" might have been material to plaintiffs' performance. Moreover, plaintiffs' submissions and the trial court's own opinion make absolutely clear that the contractors claim to have been denied specific, highly classified information, not a general warning.

Second, if plaintiffs' superior knowledge claim could not be tried without jeopardizing state secrets, the proper result would be to dismiss that claim, not to grant it without trial. The trial court's ruling, however, effectively awards plaintiffs most of what they had asked for in their superior knowledge claim – equitable adjustments that completely eliminate their serious loss position from consideration. The only thing plaintiffs have been denied is profits, which they never would have made even if the Secretary had granted their request for Pub. L. No. 85-804 relief and restructured the contract. The trial court's ruling thus improperly penalizes the government for its legitimate assertion of the state secrets privilege by disregarding the substantial losses that plaintiffs certainly would have incurred in completing the contract.

A. Plaintiffs' Superior Knowledge Claim Fails As A Matter Of Law Because The Navy Had No Duty To Disclose Highly Classified National Security Information

The basis of the superior knowledge claim contained in Count IX of the complaint is that the government improperly failed to disclose to plaintiffs highly classified information, including information contained in special access programs operated by the Air Force. Because there is no implied duty to disclose information of this kind, plaintiffs' claim fails as a matter of law.

1. Access to classified information is governed by detailed regulatory restrictions, *see, e.g.*,

Exec. Order 12958, 60 Fed. Reg. 19825 (1995); Exec. Order 12356, 47 Fed. Reg. 14874 (1982) (superseded 1995); 32 C.F.R. §§ 154 *et seq.*; *id.* §§ 159a *et seq.*, and unauthorized disclosure of such information is prohibited by stiff criminal penalties. 18 U.S.C. § 798; *see id.* §§ 793; *United States* v. *Morison*, 844 F.2d 1057, 1063-76 (4th Cir.), *cert. denied*, 488 U.S. 908 (1988). Within this framework, compartmentalized "special access programs," which included portions of the B-2 and F-117 aircraft programs, *see* 37 Fed. Cl. at 276, J.A. 218, are subject to particularly strict regulation. 32 C.F.R. §§ 159a.80-159a.89; *see id.* § 159a.9(jj). Protecting classified information from disclosure is a quintessential responsibility of the executive branch. *Department of the Navy v. Egan*, 484 U.S. 518, 527 (1988).

In the case of the typical government contract, it may be logical in some circumstances to infer that the government has agreed to disclose vital information necessary to prevent the contractor from unwittingly pursuing a "ruinous course of action." *Helene Curtis Indus., Inc.* v. *United States*, 312 F.2d 774, 778 (Ct. Cl. 1963). *See also GAF Corp.* v. *United States*, 932 F.2d 947, 949, 953-54 (Fed. Cir. 1991), *cert. denied*, 502 U.S. 1071 (1992).

However, where the information at issue is classified, no such inference is permissible. Indeed, the very statutes and regulations that restrict access to such information preclude such an inference. The strict security requirements governing classified information would be undermined if an agreement to

disclose such information could be implied simply "from the circumstances of contracting." *See Hercules, Inc.* v. *United States*, 516 U.S. 417, 429 (1996). It is unsurprising, therefore, that no court has ever found that the government has a duty to disclose such information to its contractors. The limits on access to highly classified information are a matter within the Executive's discretion that cannot be circumscribed by an "implied duty" to provide the information.

In addition, the A-12 contract specifically identified information that the government agreed to provide to the contractors. *See* J.A. 25,526-28 (A-12 Contract, Attachment 36, Section 1 ("Government Furnished Information")). This express provision leaves no room for a court to imply a contractual duty to disclose other, highly classified, information not listed.

Plaintiffs' argument that the Navy had a contractual obligation to disclose compartmentalized information concerning entirely separate programs operated by the Air Force is flatly at odds with common sense. The very reason that the A-12 program and the separate Air Force programs were compartmentalized was to maintain security and preclude broader dissemination of the information contained within each program. When the contractors entered into the A-12 contract, they knew that information regarding other low-observable weapons systems was sealed in other compartmentalized programs. *See* J.A. 68,402 (Complaint). And the A-12 contract nowhere gives

the contractors the right to insist that the Navy obtain from the Air Force, and disclose to the contractors, information regarding other compartmentalized programs.

2. The trial court nevertheless refused to dismiss plaintiffs' superior knowledge claims because, in its view, the government had a duty to provide the contractors with "at least a 'general warning' about problems concerning production of the [A-12] aircraft." 37 Fed. Cl. at 275 n.7, J.A. 217 (quoting 27 Fed. Cl. 204, 206 (1992), J.A. 29-34).

a. In discovering a duty to provide a "general warning," the trial court placed exclusive reliance on *J.A. Jones Constr. Co.* v. *United States*, 390 F.2d 886 (Ct. Cl. 1968). That decision provides no support whatever for the trial court's ruling.

In *J.A. Jones*, the Court of Claims held the government liable under the superior knowledge doctrine in a case in which a government contactor sought to recover overtime wages incurred in constructing several facilities at Cape Canaveral for an Air Force Inter-Continental Ballistic Missile (ICBM) program. 390 F.2d at 886-87. The contractor complained that the government had failed to disclose that the contractor's project was only the first of a series of ICBM construction projects in the same location, projects which resulted in a severe labor shortage and ultimately in the need to pay additional compensation. *Id.* at 887.

The Court of Claims stated that the government "was not free, if it was aware of the impending avalanche and knew that J.A. Jones was

not, to stand aside and let the bidder be overwhelmed without a warning." *Id.* at 888. In reaching this conclusion, the court declined to credit the government's concern that "disclosure by the Air Force might have adversely affected its operations," rejecting the notion that there were "any obstacles preventing the Air Force from disclosing, at least in general terms, its plans." *Id.* at 893. The court explained that "the evidence falls far short of proving that a general warning to plaintiff would have rent the security blanket." *Ibid.*

J.A. Jones does not remotely suggest that the government has an obligation to give even a general warning when doing so would conflict with security requirements. 390 F.2d at 893 n.14. In that case, the government could simply have warned the contractor of an impending labor shortage without specifying the reasons. No comparable general warning of the kind that might have been given in *J.A. Jones* could have been given in this case.

Indeed, the trial court made no attempt to explain how *J.A. Jones* could be analogized to the present case. The court did not explain what sort of "general warning" the government was required to provide and never explained how such a warning, in the context of a special access program, could be anything other than a disclosure of classified information that would have "rent the security blanket." *J.A. Jones*, 390 F.2d at 893. Nor did the court suggest how a "general warning" could have had any material impact on the contractors' bid or contract performance. It is well settled that even

where a "a party demonstrates the nondisclosure of superior knowledge, the party must still show reliance and injury by the failure to disclose." *Miller Elevator Co.* v. *United States*, 30 Fed. Cl. 662, 676 (1994) (citing *J.A. Jones*, 390 F.2d at 893), *appeal dismissed*, 36 F.3d. 1111 (Fed. Cir. 1994) (Table).

b. Despite the trial court's unexplained invocation of the "general warning" rubric, its own opinion and plaintiffs' submissions make clear that a "general warning" is not the basis of plaintiffs' superior knowledge count. Rather, plaintiffs claim that the government should have given them detailed information from other highly classified programs, including especially the B-2 and F-117 aircraft programs operated by the Air Force.

In their submissions, plaintiffs expressly acknowledged that they had received access to some information from the B-2 and F-117 programs, but complained that "the information actually provided [was only] general in nature," J.A. 68,559 (Farr Declaration), and that neither the Navy nor the Air Force "disclose[d] * * * details" (J.A. 68,559) or "provided the Contractors with specific information" (J.A. 68,560). Indeed, plaintiffs took pains to emphasize that the "[o]verview and conceptual information" given to them was only "of minimal use" precisely because "*[t]he vital information necessary [was] at the detailed level.*" J.A. 68,554 (emphasis added).

For example, plaintiffs complained that "[d]uring the B-2 briefings which we received * * *, we were told that the B-2 had significant weight

growth problems during development *[but] we were not given, nor have we ever received, details* * * *. Had [we] known and understood the *details* * * * of B-2 weight growth, our approach to the A-12 design development would have been substantially modified." J.A. 68,567-69 (emphasis added). Similarly, plaintiffs insisted that general knowledge regarding materials used in other programs was "of minimal value"; it was "detailed information" that was "vital." J.A. 68,554. Likewise, plaintiffs asserted, "the simple knowledge of the use of a given component on the B-2 [was] not enough; *detailed knowledge* of [the integration] of that component into the B-2 airframe [was] equally as critical." J.A. 68,554-55 (emphasis added). *See also, e.g.*, J.A. 68,556-57, 68,558, 68,573 (further elaborating upon highly specific and detailed nature of B-2 and F-117 information that the contractors claimed to have sought and needed); J.A. 68,581-84 (Jackson Declaration) (same).

The trial court's opinion also makes clear that plaintiffs were seeking specific, highly detailed, highly classified information. As the court recognized, their superior knowledge claim is based on the assertion that the government should have disclosed particular classified information including "weight estimation techniques, application of low-observable technologies, propulsion system technologies, composite materials and composite manufacturing technologies, and avionics technologies." 37 Fed. Cl. at 274, J.A. 216. It was detailed knowledge about these matters, not a warning phrased in general terms that allegedly

would have allowed the contractors to "solve technical problems without conducting extensive, often duplicative efforts at great expense." *Ibid.*

The attempt to save plaintiffs' superior knowledge claim by recasting it as a denial of a "general warning," is not merely at odds with plaintiffs' submissions and the trial court's own statements, but with the most basic common sense. As the contractors themselves proclaimed in their best and final offer (J.A. 35,829), they are two of this country's most experienced aircraft manufacturers. Before submitting their bid to design and building the A-12, the contractors had already spent years acquiring extensive experience in the "concept formulation" and "demonstration/validation" phases of the A-12 program, which had enabled them to study and test various proposed designs before committing themselves to construction and delivery of a specific aircraft configuration. *See* J.A. 35,811, 35,813-16, 35,821, 35,831. And, as the trial court itself recognized, it was possible that the contractors "did not lack knowledge about low-observable technology" through their involvement with other government programs. 37 Fed. Cl. at 280, J.A. 222.

Finally, even if plaintiffs' superior knowledge claim did not fail as a matter of law, it would have been necessary for the trial court to consider all the evidence of information made available to the contractors before finding that the government had failed to provide a "general warning." The absence of a hearing and findings on such fundamental considerations would itself require reversal.

B. The Government's Proper Invocation Of The State Secrets Privilege Did Not Require It To Pay All Of Plaintiffs' Incurred Costs Regardless Of Their Projected Losses

It was also plain error for the trial court to bar application of a loss ratio on the ground that it could not try plaintiffs' superior knowledge claim without threatening the disclosure of state secrets.

As the cases recognize, the proper response to a valid invocation of the state secrets privilege which prevents further litigation of the issues is dismissal of the plaintiffs' claims. *Kasza* v. *Browner*, 133 F.3d 1159, 1170 (9th Cir. 1998); *Bareford* v. *General Dynamics Corp.*, 973 F.2d 1138, 1141 (5th Cir. 1992), *cert. denied*, 507 U.S. 1029 (1993); *Ellsberg* v. *Mitchell*, 709 F.2d 51, 65 (D.C. Cir. 1983), *cert. denied*, 465 U.S. 1038 (1984); *Zuckerbraun* v. *General Dynamics Corp.*, 935 F.2d 544, 547 (2d Cir. 1991). *See also Molerio* v. *FBI*, 749 F.2d 815, 825 (D.C. Cir. 1984) (upholding dismissal of plaintiff's claim where invocation of state secrets privilege prevented government from litigating a valid defense). In no instance has the government been penalized for invoking a privilege to protect matters vital to the national security.

Indeed, it is the settled rule that "in a civil forum where the Government is not the moving party, but is a defendant only on terms to which it has consented," *United States* v. *Reynolds*, 345 U.S. 1, 12, (1953), the government cannot be "punished for asserting the privilege." *Salisbury* v. *United*

States, 690 F.2d 966, 975 (D.C. Cir. 1982). *See In re United States*, 872 F.2d 472, 476 (D.C. Cir.), *cert. dismissed*, 493 U.S. 960 (1989) ("Notions of sovereign immunity preclude any further adverse consequence to the government, such as alteration of procedural or substantive rules").

Accordingly, under settled law, because plaintiffs could not try their Count IX superior knowledge claim without jeopardizing state secrets, it would have been necessary to dismiss that claim even if it did not fail as a matter of law.

In a misguided effort to "spread the consequences" of its inability to hold a trial, 37 Fed. Cl. at 285, J.A. 227, the trial court awarded the contractors all of their incurred costs – despite their performance failures and their acknowledge loss position. The court was plainly wrong: it effectively imposed a massive penalty on the government for asserting the state secrets privilege to protect national security. In this case, application of the appropriate loss ratio would have eliminated plaintiffs' damages altogether or, at least, should have reduced plaintiffs' recovery to a fraction of their incurred costs.[5] Instead, in awarding plaintiffs their incurred costs and disregarding their loss position, the court's order shifts the contractors' losses to the government. Indeed, the order has the effect of

[5] Although the contractors insisted that they should recover without regard to their loss position, they aggressively applied substantial loss ratios to their subcontractors. *See, e.g.*, J.A. 68,653-54 (Yochum Dep.); J.A. 10,560-62 (Robert Wright); J.A. 12,877-78 (Alan Broesche).

putting the contractors in a far better position by defaulting and provoking a termination than they would have been in if their request for restructure – which recognized that they could have no expectation of profit, J.A. 18,217 (proposing to assume a $1.5 billion loss) – had been granted by the Secretary.

* * * *

REPLY/CROSS-APPELLEE BRIEF FOR
DEFENDANT-APPELLANT UNITED STATES

IN THE UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

No. 98-5096, -5122, 5123

McDONNELL DOUGLAS CORPORATION,

Plaintiff-Cross Appellant,

and

GENERAL DYNAMICS CORPORATION,

Plaintiff-Cross Appellant,

v.

UNITED STATES,

Defendant-Appellant.

APPEAL FROM THE UNITED STATES
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SEPTEMBER 28, 1998

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* * * *

II. THE TRIAL COURT ERRED IN AWARDING THE CONTRACTORS THEIR INCURRED COSTS

Summary. As we have shown, the conversion to a termination for convenience must be reversed and the award of damages must therefore be vacated. Assuming, however, that the Court were to address the trial court's damages ruling, reversal of this ruling would be required as well, for two independent reasons.

First, plaintiffs have never articulated how the government could have had a superior knowledge duty to disclose highly classified information regarding virtually every aspect of contract performance, and they do not do so now.

Second, wholly apart from the merits of plaintiffs' superior knowledge claim, dismissal would be required under settled state secrets doctrine. When a claim cannot go forward without jeopardizing state secrets, the rule is clear: the claim is dismissed and is removed from the case. Under settled law, therefore, when the trial court determined that it could not try plaintiffs' superior knowledge claim, it was required to dismiss that claim. Plaintiffs have the burden of proving the validity and amount of their claimed equitable adjustments. Their inability to prove these claims does not preclude the government from establishing the estimated cost at the completion of the contract, the only issue on which it bears the burden of proof.

In their cross-appeal, plaintiffs argue that, contrary to the trial court's ruling, they can try their superior knowledge claim without endangering state secrets, and also assert that they have other triable claims that might entitle them to an equitable adjustment. Pl.Br. 60 & n.43. Plaintiffs offer no basis for overturning the trial court's conclusion that it could not try their superior knowledge claims without endangering state secrets. And their assertion that they can pursue claims for equitable adjustments on the basis of alternative theories that might not jeopardize state secrets only highlights the error of the judgment they seek to defend.

A. This Case Presents No Viable Superior Knowledge Claim

1. Plaintiffs do not seriously argue that they had a right to receive classified information under the superior knowledge doctrine. *See* Gov't Br. 39-41; Pl.Br 43, 44. Plaintiffs' failure to demonstrate a right to classified information is fatal to their superior knowledge claim. Plaintiffs argue, however, that they had a right to a "general warning" that would not itself divulge classified information, relying on *J.A. Jones Constr. Co. v. United States*, 390 F.2d 886 (Ct. Cl. 1968).

That reliance is fundamentally misplaced. In *J.A. Jones*, a contractor recovered overtime wages paid in constructing facilities at an Air Force missile test center at Cape Canaveral. *See* 390 F.2d at 886-87. The sole issue was whether the government should have given the contractor some warning that its labor costs would likely be higher than normal

because the government was at the same time planning to undertake a large number of projects in the vicinity. *Id.* at 887. The *J.A. Jones* court held that there was a duty to give such a warning, rejecting the contention that security concerns compelled nondisclosure, because "the evidence [fell] far short of proving that a general warning to plaintiff would have rent the security blanket." 390 F.2d at 893 n.14.

Plaintiffs suggest that, in this case, the government could have warned them generally about the "unique weight-growth history of low-observable aircraft, without disclosing any classified information." Pl.Br. 47. But plaintiffs do not explain how a "warning" about the "unique weight-growth history of low-observable aircraft" could have been framed in a way that would not have revealed classified information.

In any event, plaintiffs' own pleadings establish that this kind of warning has nothing to do with their claim. The government informed plaintiffs six months before they signed the A-12 contract that their proposed aircraft would be more than 2800 pounds over-weight. J.A. 14,940, 14,942. In addition, plaintiffs' principal declaration admits that they were ultimately "told that the B-2 experienced weight growth well beyond estimates." J.A. 68,567 (Farr Decl.). But the same declaration makes clear that plaintiffs believed such a warning was useless: "we were not given, nor have we ever received, *details* of the B-2 weight histories * * *." *Ibid.* (emphasis added); *see* Gov't Br. 44.

The trial court opinion as well as plaintiffs' complaint and Count IX summary judgment motion all make clear that plaintiffs had no use for a "general warning." Instead, as we showed at length in our opening brief (Br. 43-46), what plaintiffs allege they did not receive was a wide range of specific, detailed information regarding the development, design, and construction of the B-2 and F-117 aircraft, including such matters as weight-estimation techniques, application of low-observable technologies, propulsion system technologies, composite materials and composite manufacturing technologies, and avionics technologies. J.A. 68,401-04, 68,413, 68,417-19, 68,420; *see also, e.g.*, J.A. 68,554-60 (Farr Decl.).[8]

Plaintiffs suggest that as an alternative to providing a general warning, the government could have "structur[ed] the contract to take account of its superior knowledge * * * without revealing any classified information." Pl.Br 43-44. Plaintiffs urge that the government could have "specif[ied] a longer contract development schedule," or "a different range of performance specifications," or insisted upon "a

[8] Plaintiffs themselves concede that once the contract was awarded, it may be that "the only way the government could have fulfilled its duty * * * was to disclose that information to plaintiffs." Pl.Br. 47 n.31. Plaintiffs thus acknowledge that the superior knowledge that they allegedly required was detailed, classified information, not a "general warning." As discussed, however, plaintiffs never respond to the showing in our opening brief that they had no right, contractual or otherwise, to receive this highly classified information.

cost-type contract for some or all of the contract effort." Pl.Br 47.

The sole authority cited for this contention is the suggestion in *J.A. Jones* that the government, as an alternative to providing a general warning, might have included a "price-escalation clause" to cover the eventuality of increased labor costs in the project area. 390 F.2d at 893. This suggestion fails for the same reason as plaintiffs' reliance on a "general warning" theory. The *J.A. Jones* court suggested only that general warnings and price-escalation clauses may be sensible devices for communicating discrete unclassified information to contractors. These devices have no conceivable application where, as here, plaintiffs' claim is that the government should have provided classified information regarding a broad range of critical aspects of contract performance.[9]

[9] Indeed, the sheer breadth of information sought by plaintiffs would appear to take their claims out of the superior knowledge doctrine altogether. That doctrine, in some instances, requires the government to disclose a discrete, identifiable piece of information vital to contract performance. *See, e.g., Hardeman-Monier-Hutcherson* v. *United States*, 458 F.2d 1364 (Ct. Cl. 1972) (reports relating to adverse weather and sea conditions); *Helene Curtis Indus., Inc.* v. *United States*, 312 F.2d 774, 778 (Ct. Cl. 1963) (particulars of grinding process necessary to contract performance). Plaintiffs here would extend that duty to make the government a guarantor of their knowledge on a wide range of matters relating to the design and manufacture of the aircraft they had agreed to build. But the superior knowledge has never been held to sweep so broadly, and the government was entitled, in awarding the contract, to rely on

Plaintiffs never explain how a "price escalation" clause could operate in the circumstances of this case. Instead, plaintiffs would transform the court's allusion to a price-escalation clause into a sweeping duty to rewrite contract bids in the most fundamental and all-encompassing way. *J.A. Jones* provides no support for this novel theory, and the trial court at no time suggested that plaintiffs were entitled to a different contract than the one they had agreed to.

At bottom, plaintiffs seek to defend the trial court's insupportable superior knowledge rationale on the basis of claims that have never been addressed. Plaintiffs assert in a number of counts in their complaint that the government knew that contract performance was impracticable or made it so by failing to provide necessary information. They argue that they are entitled to reformation because the contract was impossible or impracticable to perform, Counts VI & VII, J.A. 68,442-46, and because the contract as written resulted from a mutual mistake of fact about the contract's difficulty of performance, Count VIII, J.A. 68,446-47. And in Count X, plaintiffs argue that the government failed to provide the cooperation and information it had promised or should have provided. J.A. 68,449-50. But none of these claims has ever been tried. Plaintiffs cannot prevail unless they demonstrate that there is a basis in law and fact for the relief they seek. They have not done so here.

plaintiffs' claims of expertise. *See generally American Ship Building Co.* v. *United States*, 654 F.2d 75, 79 (Ct. Cl. 1981).

2. Plaintiffs not only purport to have stated a viable superior knowledge claim that should withstand a motion to dismiss; they further argue that they have demonstrated a "prima facie" case. *See* Pl.Br 48. Conspicuously, plaintiffs never identify the factual basis of this prima facie case.

Plaintiffs' extended comparison of their bid with that of the Northrop team (Pl.Br. 45-47) does not advance their argument. Plaintiffs argue that the government should have known from the Northrop team's bid that plaintiffs lacked necessary knowledge. But the designs prepared by the two teams were different in crucial respects and cannot be compared in the simplistic fashion proposed by plaintiffs.[10] Plaintiffs suggest, for example, that the government should have known that the plaintiffs' proposed weight specifications were unattainable because they were lower than Northrop's. *See* Pl.Br. 45. But "[t]he aircraft design proposed by [plaintiffs] was very different than that of the Northrop team." J.A. 69,326 (Cate Decl.). Thus, "[w]hile there were qualitative similarities between the designs (both were low observable designs and both proposed the use of composites), there was no direct correlation between the two weight estimates because of the many, weight-critical, differences in configuration, materials, propulsion systems, avionics, and other fundamental design features that influence aircraft weight." J.A. 69,327 (Cate Decl.).

[10] Plaintiffs do not suggest that the government should have disclosed the contents of Northrop's bid; such disclosure would have violated the law. *See* 41 U.S.C. § 423; 48 C.F.R. § 3.104.

Nor can plaintiffs premise a superior knowledge claim on the ground that they were the low bidder. Cost estimates reflected two unique designs. J.A. 69,329-30 (Popp Decl.). Thus, "the fact that Northrop proposed a higher price for its FSED aircraft design has absolutely no bearing on the question of whether [plaintiffs] may have priced [their] FSED design too low." J.A. 69,331.[11]

It may be that plaintiffs are relying on the trial court's "Classified Appendix" to identify their "prima facie" case. As discussed in our opening brief (Br. 48-50), such reliance would be manifestly improper. The problem is not, as plaintiffs suggest, that the trial court issued a classified opinion, but that the court has improperly refused to disclose the opinion to the executive branch on national security grounds. *See generally Department of the Navy* v. *Egan*, 484 U.S. 518, 527 (1988). Moreover, a court cannot include in a secret record documents not submitted by either party. *See* J.A. 262-63. In effect, this Court has been asked to affirm the trial court judgment on the basis of an opinion that the United States has not been permitted to see. We are

[11] Contrary to plaintiffs' suggestion (Pl.Br. 47), numerous witnesses testified in their depositions that the A-12 was *not* envisioned simply as "a shrunken version of the B-2," J.A. 69,362 (Miller), or "a miniature B-2." J.A. 69,360 (Chu). *See also* J.A. 69,364 (Schumacher) (rejecting suggestion that the A-12 was "supposed to be a mini B-2"). And since no trial was held on Count IX and no witness testified at the Count XVII trial regarding the relationship (if any) between the A-12 and the B-2, the current record provides no basis whatsoever for any finding on this matter.

aware of no precedent, and plaintiffs cite none, for such an extraordinary request.[12]

3. Finally, as urged in our opening brief (Br. 46), even if plaintiffs' superior knowledge claim did not fail as a matter of law, it would have been necessary for the trial court to consider all the evidence of information made available to the contractors in order to determine whether, in fact, the government failed to provide a "general warning." The government filed in the trial court not only an initial motion to dismiss but also a subsequent motion in the alternative for summary judgment urging, *inter alia*, that the Navy afforded plaintiffs an opportunity to obtain particular B-2 information directly from Northrop but that plaintiffs deliberately declined to avail themselves of this opportunity for internal business reasons. *See* J.A. 69,333-34, 69,336-40; *see also* J.A. 69,345-47. Resolution of these crucial issues would clearly be required even if it were determined that plaintiffs' claim could survive a motion to dismiss.

[12] Of course, this Court can properly review the classified materials submitted by the parties, such as the classified, *in camera* declarations supporting the state secrets privilege. *See* J.A. 69,367-69. But, contrary to plaintiffs' assertions (Pl.Br. 62-63), documents were not properly made part of the record by the United States merely because the court may have obtained them from court security officers who are government employees.

B. That The State Secrets Privilege Would Prevent Plaintiffs From Proving Their Superior Knowledge Claim Does Not Preclude The Government From Showing That They Were In A Loss Position

1. As we showed in our opening brief, reversal of the trial court's damages calculation would be required even if plaintiffs' superior knowledge claim were sufficient to withstand the government's motions to dismiss and for summary judgment. When a plaintiff cannot try its claim without jeopardizing state secrets, that claim – even if otherwise viable -- must be dismissed and removed from the case. *See, e.g., Kasza* v. *Browner*, 133 F.3d 1159, 1166, 1170 (9th Cir. 1998), *petition for cert. filed*, No. 98-5405 (U.S. July 23, 1998); *Bareford* v. *General Dynamics Corp.*, 973 F.2d 1138, 1141 (5th Cir. 1992), *cert. denied*, 507 U.S. 1029 (1993); *Zuckerbraun* v. *General Dynamics Corp.*, 935 F.2d 544, 547 (2d Cir. 1991); *Ellsberg* v. *Mitchell*, 709 F.2d 51, 64-65 (D.C. Cir. 1983), *cert. denied*, 465 U.S. 1038 (1984). That is the result even if a plaintiff can make out a prima facie case with unprivileged material. *See, e.g., Bareford*, 973 F.2d at 1143 ("[e]ven if we found that [plaintiffs] had made out a prima facie case with unprivileged information, * * * the state secrets doctrine would nonetheless bar the * * * action").

Plaintiffs do not question the correctness of any of these cases, and cite no case in which a claim that could not be pursued without jeopardizing state

secrets was left in the case. They do not dispute that they bear the burden of proving their superior knowledge claim. Manifestly, that claim must thus be dismissed under state secrets doctrine even if it were otherwise viable.

Plaintiffs seek to avoid the application of settled law by arguing that if they cannot litigate their superior knowledge claims, the government should be precluded from establishing the applicable loss ratio. But plaintiffs indisputably bear the burden of proving both the validity and the amount of their claims for equitable adjustments, including those based on superior knowledge. *See* John Cibinic, Jr. and Ralph C. Nash, Jr., *Administration of Government Contracts* 698 (3d ed. 1995) ("In establishing the total amount of an equitable adjustment, the burden of proof is allocated to the party that is claiming the benefit of the adjustment.").

If plaintiffs cannot carry that burden without jeopardizing state secrets, there is simply no upward adjustment to the contract price. Plaintiffs' inability to try their claim does not preclude the government from meeting its burden as to loss ratio. The government can demonstrate plaintiffs' actual losses by establishing the total estimated cost at the completion of the contract and demonstrating that it would substantially exceed the contract ceiling price. *See* 48 C.F.R. §§ 49.203(c)(2). And the government indisputably can do so without jeopardizing state secrets. Plaintiffs' argument simply seeks to keep in the case claims that must be dismissed under state

secrets doctrine and to use those claims to frustrate the government's ability to try its case.

The trial court concluded that it would be a "sham" to permit the government to demonstrate a loss ratio when plaintiffs could not, by operation of the state secrets privilege, try their superior knowledge claims. 37 Fed. Cl. at 285, J.A. 227. It is no less a sham to allow plaintiffs to recover their incurred costs as reflecting their actual damages, while precluding the government from proving the applicable loss ratio. The trial court's ruling simply shifts the impact of plaintiffs' inability to try their claim from plaintiffs to the government.

2. Plaintiffs urge that a trial court has equitable discretion to "spread[] the consequences" resulting from the assertion of the state secrets privilege. *See* 37 Fed. Cl. at 285, J.A. 227. But plaintiffs offer no authority for their contention, and they cite no case in which a court has refused to dismiss a claim which could not be tried for state secrets reasons. The reason for this utter absence of support for plaintiffs' proposal is plain. The government does not assert the state secrets privilege to protect its litigation interests. The state secrets privilege exists to protect matters crucial to the national security, and it may be necessary to invoke the privilege even where doing so is contrary to the government's litigating interests. *See Molerio* v. *FBI*, 749 F.2d 815, 825 (D.C. Cir. 1984). Because the privilege operates neutrally to protect national security concerns, the cases uniformly hold that a

claim that jeopardizes state secrets must be dismissed.

The application of the state secrets privilege is often harsh, but no court has thought that it could leave a barred claim in the case to "spread[] the consequences." Notably, General Dynamics itself has been the beneficiary of this rule. The plaintiffs in *Bareford* and *Zuckerbraun* brought major tort actions against General Dynamics. The government intervened and obtained dismissal of the suits because trial would have jeopardized state secrets. The dismissals did not reflect a determination that the claims were legally defective; indeed, the court in *Bareford* stressed that it was irrelevant whether plaintiffs could demonstrate a prima facie case. *Bareford*, 973 F.2d at 1143. Nor was dismissal of those suits thought to be "equitable." Dismissal was simply necessary. That is equally true here.

3. In any event, the suggestion that the result here is in any sense equitable or that it "spreads the consequences" cannot be taken seriously. Plaintiffs do not dispute that as a result of the trial court's treatment of their superior knowledge claim they are in a far better position than they would have been in if Secretary Cheney had accepted their proposal to restructure, under which they would have assumed a $1.5 billion loss. J.A. 18,217. By leaving the superior knowledge claim in the case, the court gave plaintiffs all or virtually all the relief they could have obtained had they carried their burden of proof on that claim at trial. This result cannot possibly be characterized as

"equitable." And, of course, it is hardly "equitable" to preclude application of a loss ratio when, as discussed in our opening brief (Br. 47 n.5), plaintiffs aggressively applied loss ratios to their subcontractors.

4. In their cross-appeal, plaintiffs suggest that they can prove their equitable adjustments based on other theories that remain in the case, and also urge that they might be able to try their superior knowledge claim without jeopardizing state secrets. Pl.Br. 60 & n.43. Plaintiffs offer no basis whatsoever for overturning the trial court's conclusion that their superior knowledge claim cannot be tried without jeopardizing state secrets.

Plaintiffs' argument that their alternative claims might support their request for equitable adjustments simply underscores the error of the judgment at issue. The premise of the trial court's ruling is that plaintiffs could not try their claims. That premise fails if plaintiffs can try their claims on other theories. Before precluding the government from establishing a loss ratio, the court should plainly have considered whether plaintiffs' alternative claims would permit trial of their requests for adjustments without jeopardizing state secrets.

* * * *

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	
	)	No. 91-1204C
v.	)	(Judge Hodges)
THE UNITED STATES,	)	
Defendant.	)	

DEFENDANT'S STATEMENT OF ISSUES AND NOTICE OF PROBABLE TESTIFYING EXPERTS FOR TRIAL

Pursuant to the Court's direction and the agreement of the parties reached on June 27, 2000, defendant, the United States, provides the following summary of issues that it intends to present at a trial to determine whether plaintiffs, McDonnell Douglas Corporation and General Dynamics Corporation, were in default of their contractual obligations. *See McDonnell Douglas Corp. v. United States*, 182 F.3d 1319, 1329 (Fed. Cir. 1999); *see also id.* at 1332-33. We also identify the expert witnesses whom we currently intend to call to testify in support of our case regarding liability and damages. In addition, although not required by the Court's

direction, we include a statement of our tentative responses to plaintiffs' anticipated affirmative defenses.

We regard our case development as substantially completed; however, as the Court is aware, we require a modest amount of time to complete additional, focused discovery. Accordingly, the following positions and identification of testifying witnesses could warrant change based upon additional discovery; plaintiffs' own identification of their affirmative defenses, damages positions, and testifying experts; or other developments.

* * * *

II. ANTICIPATED AFFIRMATIVE DEFENSES

Although we await the contractors' statement regarding their affirmative defenses to default, we anticipate that, given the current posture of the litigation, the contractors' remaining defenses essentially can be reduced to three excuses: (a) the Navy's alleged waiver of the contract's weight and schedule requirements; (b) the Navy's alleged withholding of superior knowledge; and (c) the alleged impossibility of the contract's specifications. Below, we address briefly each of these anticipated defenses.

A. Waiver

It is settled that the Navy's undisputed desire "to preserve the program and its A-12 aircraft" at

termination does not mean "that Contractors were not in default under the contract, or that the government did not have the right to terminate the contract for default." *McDonnell*, 182 F.3d at 1327. Further, "[a] party that chooses to proceed with the contract -- even if it is the government, and even if it manifests a strong desire to procure the item that is the subject of the contract -- does not thereby waive its right to terminate for default." *Id.* Thus, to excuse their default by reason of waiver, the contractors must establish that the Navy specifically waived its right to enforce each and every guaranty or specification as to which the contractors were failing to make progress at termination. We will demonstrate at trial that the contractors' burden in this case is extraordinarily heavy, and one that they cannot meet.

We understand the contractors' waiver defense to have two essential components: (1) the Navy allegedly waived all but two grounds for default (failure to meet the contract's weight and schedule requirements) due to the manner in which the Navy crafted its cure notice; and (2) the Navy allegedly also waived the only two grounds for default supposedly identified in its cure notice.

As an initial matter, the issue of waiver has never been "fully litigate[d]." *McDonnell*, 182 F.3d at 1332. Thus, there is not a complete record upon which to predicate a final ruling regarding the issue of waiver. Indeed, the first part of the contractors' expected waiver argument highlights the incomplete state of the current record. First, as a matter of fact,

the cure notice explicitly identified four bases for default (schedule, inability to manufacture composite parts, weight, and carrier suitability requirements), not two (weight and schedule) as claimed by the contractors. Second, even if the contractors' cramped reading of the cure notice were correct, as a matter of law, the cure notice simply does not circumscribe the grounds upon which the Government may sustain the default. *Eg., Kelso v. Kirk Bros. Mech. Contractors, Inc.*, 16 F.3d 1173, 1175 (Fed. Cir. 1994) (citing *Joseph Morton Co. v. United States*, 757 F.2d 1273, 1277 (Fed. Cir. 1985)); *Composite Laminates, Inc. v. United States*, 27 Fed. Cl. 310, 318 (1992). We will demonstrate at trial that the Navy provided the contractors with notice of the various areas in which they were failing to make progress so as to endanger contract performance. The notice issue alone raises genuine factual disputes requiring resolution.

As to the Navy's alleged waiver of the weight guaranty, we will demonstrate at trial that the contracting officer repeatedly reserved, in writing and orally, the Government's right to terminate for default for the contractors' failure to meet the contract specifications, including the weight guaranty. The contractors, then two of the nation's largest and most experienced Government contractors, were well aware of the rules regarding modification and relaxation of contract specifications. As the Court has observed already, the Navy's "strategy was to maintain the original contract until the end, then exact consideration for the contractors'

failure to meet the BAFO weight." *McDonnell IV*, 35 Fed. Cl. at 373. Because, as we will establish at trial, the contractors were aware of the Navy's intent to exact consideration, the contractors cannot demonstrate that they detrimentally relied upon any purported waiver of their weight guaranty. *See Indemnity Ins. Co. v. United States*, 14 Cl. Ct. 219, 226 (1988) (forbearance not a waiver if government "made it clear it was not waiving any contract right").

We understand the contractors' argument regarding schedule waiver to be fundamentally different than their argument regarding weight waiver. Rather than contending that they relied to their detriment upon an alleged waiver of the contract schedule, the contractors claim that the Navy botched its attempt to maintain an enforceable schedule when it granted the contractors a unilateral extension of 18 months to achieve first flight. According to the contractors, the revised schedule contained in contract modification P00046 was "unreasonable," and, as a result, there was no enforceable schedule in place at termination. At trial, we will demonstrate that the Navy selected the December 1991 first flight date imposed by P00046 because it was within the range of dates that both the contractors and Navy program management leadership identified as reasonable and achievable. Indeed, at the time the Navy issued P00046, the contractors represented that first flight would occur sooner than the 18-month extension granted in P00046.

Finally, in no event would the waiver as alleged previously by the contractors excuse all of their defaults, including General Dynamics' inability to manufacture composite parts, the contractors' predicted failure to meet the contract's performance specifications, the flaws in the propulsion design, or the structural insufficiency of the aircraft's design. More fundamentally, waiver would not entitle the contractors to any equitable adjustments in the contract price; thus, it would not excuse their financial inability to perform the contract without extraordinary relief. In short, under no circumstances could waiver of the contract's weight and schedule requirements -- even if established -- excuse the contractors' default.

B. Superior Knowledge

We also expect the contractors to maintain that the Navy breached a duty to disclose "superior knowledge" in its possession (derived primarily from the Air Force's B-2 and F-117A classified programs) that supposedly would have been critical to the contractors in performing the A-12 FSD contract. To establish their superior knowledge excuse, the contractors must demonstrate that: (1) they undertook to perform without vital knowledge of a fact that affects performance, costs, or duration; (2) the Navy was aware that they had no knowledge of, and had no reason to obtain, such information; (3) any contract specification supplied misled them, or did not put them on notice to inquire; and (4) the Navy failed to provide the relevant information. *See*

American Ship Bldg. Co. v. United States, 654 F.2d 75, 79 (Ct. Cl. 1981).

At trial, we will demonstrate that any past, present, or future invocation of the state secrets privilege by the Executive would not determine necessarily the outcome of the contractors' superior knowledge claims in this case. Even assuming that the Navy was bound to provide a general statement about classified information without compromising national security, *J.A. Jones Constr. v. United States*, 390 F.2d 886, 890 (Ct. Cl. 1968),[3] and that the Air Force's knowledge of the B-2 and F-117A programs could somehow be imputed to the Navy, we will establish at trial the Navy fulfilled any such alleged duty. We will present evidence demonstrating that the Navy not only facilitated the contractors' access to information from other programs prior to award, it also warned the contractors regarding their proposed weight

[3] Although previously the Court ruled, or has indicated that it would rule, that the Navy owed the contractors an underlying duty of disclosure in this case, we respectfully disagree. As a matter of law, the Navy was never charged with any implied duty to disclose classified information to the contractors, much less the type of information at issue here, which is contained in very highly classified special access, compartmentalized programs. Absent a controlling statute, the protection of classified information is committed to the broad discretion of the Executive. *Department of Navy v. Egan*, 484 U.S. 518, 530 (1988). Moreover, even if they could be entitled to such information, the contractors never attempted to negotiate its disclosure as part of the contract's Government-furnished information clause.

guaranty and other technical requirements during the proposal stage. *See Petrochem Servs., Inc. v. United States*, 837 F.2d 1076, 1080 (Fed. Cir. 1988) (oral communications are effective notice to give rise to contractor's duty to inquire). The contractors rejected the Navy's warnings.

After award, the contractors affirmatively rejected opportunities to obtain precisely the kind of information they would later accuse the Navy of failing to provide. As to B-2 information, the contractors refused initially to engage, and then agreed to participate only reluctantly, in a technology exchange program established by the Navy A-12 Program Office and the Air Force B-2 program. The contractors were unwilling to participate in these programs because McDonnell Douglas had been engaged in litigation with Northrop regarding alleged misuse of proprietary information in connection with another program. In any event, General Dynamics' chief engineer, Keith Jackson, has acknowledged that nothing learned from the B-2 program during the time of the A-12 contract would have caused the A-12 contractors to do anything differently. As to F-117A information, we will demonstrate that the contractors represented in their final proposal that, via a subcontract, they would have access to the stealth expertise of Lockheed, the F-117A prime contractor. However, just four months after contract award, General Dynamics decided to sever its relationship with Lockheed, in part, because, according to General

Dynamics, Lockheed offered only a "marginal technical benefit."

Further, we also will demonstrate at trial that the contractors failed to avail themselves of opportunities to obtain the alleged "superior knowledge" from other contractors and other sources in the industry. Mr. Brown and John Cashen, the B-2's designer, both will testify that assistance and information was available to the contractors from other sources. Thus, even if the Air Force's knowledge of the B-2 and F-117A programs could be imputed to the Navy, the availability of information through other industry sources means that the Navy never possessed a duty to share that type of information. *See H.N. Bailey & Assocs. v. United States*, 449 F.2d 376, 382-83 (Ct. Cl. 1971).

Thus, because the contractors cannot possibly establish mandatory elements of their superior knowledge claim, the Court need not ever reach the issue of state secrets.

C. Impossibility

As a final basis to overturn the termination for default, we expect the contractors to allege that certain specifications, either individually or collectively, were impossible or commercially impracticable to achieve. To establish legal impossibility, the contractors must establish that: (1) the industry as a whole found the specifications objectively impossible; (2) the contractors took all reasonable action to perform the contract

notwithstanding the occurrence of an excuse; (3) there was a causal connection between allegedly impossible specifications and their performance; and (4) they did not assume the risk of impossibility of the specifications. *See Jennie-O Foods v. United States*, 580 F.2d 400, 408 (Ct. Cl. 1978).

As a threshold matter, the defense of legal impossibility is not available in a research and development contract because the Government does not warrant specifications when it engages a contractor to use its ingenuity to develop a new system, product, or method. *See J. A. Maurer, Inc. v. United States*, 485 F.2d 588, 594, 595 (Ct. Cl. 1973). By definition, a contractor performing research and development is doing that which, to a certain extent, has never been done before. Thus, the contractors cannot escape the risk of their bargain by seeking to excuse their failed performance upon the ground that the contract work is "beyond the state of the art."

In any event, the contractors cannot prevail upon their impossibility claim because they assumed the risk of nonperformance. To recover upon an impossibility claim, a contractor must demonstrate that the contract contained design specifications and that the Government, not the contractor, provided the design specification. *See J.A. Maurer*, 485 F.2d at 594. Moreover, where, as here, a contractor bids aggressively to get a contract knowing that performance only will be possible under ideal conditions, the contractor bears the risk of nonperformance. *See Wunderlich Contracting Co. v. United States*, 351 F.2d 956, 964 (Ct. Cl. 1965).

We will demonstrate at trial that the contractors originated the basic design for the A-12 long before award of the FSD contract; participated in the iterative development of the technical specifications for the contract, including the most critical performance requirements such as weight and signature levels; induced the Navy to discard requirements that they found difficult to achieve; participated in the development of the Navy's acquisition strategy; conducted extensive risk identification activities prior to contract award; professed to have the requisite skill and expertise for the contract; submitted an aggressive final offer with regard to cost and schedule; won the competition for the contract upon the basis of their proposed design and prior experience; and represented for two and a half years following award that they were able to perform. At bottom, the contractors entered into a fixed-price incentive contract knowing that the contract posed substantial technical and business risks, and the contractors willingly accepted these risks. In such circumstances, as a matter of law, the contractors unquestionably assumed the risk of nonperformance.

Finally, even if the contractors had not assumed the risk of nonperformance, their impossibility claim would nevertheless fail upon its merits, as the contractors cannot establish that the contract specifications were objectively impossible. To prevail, the contractors must carry their burden to prove that the industry as a whole found the specifications objectively impossible. *See Jennie-O*

Foods, 580 F.2d at 408. They cannot do this. For example, Messrs. Brown, Cashen, and Booz all will testify that the A-12's signature requirements were not beyond the state of the art at the time of contract award.

III. DAMAGES ISSUES

A. Default Damages

As a result of the contractors' default, the Government is entitled to recover approximately $1.35 billion in unliquidated progress payments, plus interest. *See* 48 C.F.R. § 49.402-2(a). In this particular case, the financial consequences to the contractors of default are not draconian. First, because the contractors successfully obtained the Navy's agreement to permit them to liquidate progress payments after design reviews (rather than requiring actual delivery of an aircraft or test article), the contractors will forever keep approximately $1.35 billion. Second, unlike other defaulting contractors, the contractors have escaped all liability for the costs borne by the Government to obtain substitutes for the A-12 aircraft. 48 C.F.R. § 49.402-2(e). Therefore, because the contract permits the contractors to retain $1.35 billion in liquidated progress payments, and the contractors incurred nearly $4 billion in costs during contract performance, the contractors will recover no less than 33 cents on the dollar if the default is sustained. That is, the default in this case still requires the taxpayers to bear the burden for one-third of the costs incurred at termination.

B. Effect Of Loss Adjustment Even If The Termination Were Converted

Although the Government's termination for default should be sustained, the same contract that permits the contractors to retain $1.35 billion in a default would require application of a loss adjustment even if the default were converted to a termination for convenience of the Government. A termination for the convenience should not put the contractors in a better position than that in which they would have been if the contract had been completed. *See* 48 C.F.R. § 49.203 (a), (c)(1)-(2) (Adjustment for Loss), 48 C.F.R. § 52.249 -2 (f)(2)(iii). It is settled that the contractors conceded as early as June 1990 that the cost of completing the contract would substantially exceed the ceiling price by a magnitude that they could not absorb, *McDonnell*, 182 F.3d at 1322, and that "as suggested cure, Contractors submitted a proposal to restructure the contract, pursuant to which Contractors would absorb a $1.5 billion fixed loss on the cost overrun from the contract, the contract would be restructured to a cost reimbursement contract, and Contractors would waive their claims for equitable adjustment." *Id.* at 1323. Indeed, the Court has recognized that "[t]he contractors' estimates [in mid-1990] showed that the projected costs would exceed the contract ceiling price by $324 million." *McDonnell IV*, 35 Fed. Cl. at 362.

Thus, the calculation of any potential convenience termination recovery must reflect these enormous losses. There is nothing unfair about this

contract requirement: the contractors themselves applied substantial loss adjustments to their own subcontractors in calculating the settlements due to those subcontractors in the aftermath of termination.[4]

In this case, the mandatory loss adjustment would reduce by well over $1 billion any potential termination for convenience recovery by the contractors. Edward J. Kelly, Division Head of Advanced Concepts Branch of the Naval Air Systems Command, is an experienced estimator of the cost of military aircraft programs. Mr. Kelly's extensive, independent review and analysis understates the likely cost that the contractors would have borne had they completed the contract. For example, Mr. Kelly assumes no major redesign, even though other Government experts will testify that major redesign was required. Similarly, independent of Mr. Kelly, experienced cost estimators at TASC, a leading firm in the estimation of major defense program costs,

[4] A "loss ratio" is first derived by dividing the contract price, plus any equitable adjustments, by the total cost estimated at completion (or "EAC"). 48 C.F.R. § 49.203(c)(2). The loss ratio is then multiplied against a contractors' recoverable costs to reduce the contractors' recovery so as to reflect the rate of loss that the contractor would have borne had the contract been completed. *E.g.*, *McDonnell Douglas Corp. v. United States* ("*McDonnell V*"), 37 Fed. Cl. 270, 273 (1996). Although the contractors have submitted claims for equitable adjustment, we are uncertain which claims, if any, they intend to pursue and upon what supporting data, if any, they intend to rely. We await the contractors' response to this statement to clarify which claims, if any, they intend to pursue.

have developed a conservative, comprehensive estimate at completion for the A-12 contract. Like that of Mr. Kelly, TASC's analysis presupposes no major technical redesign. Although these analyses are subject to change upon completion of focused discovery, they currently indicate that the cost at completion of the FSD contract would have been approximately $8.3 billion. Thus, even in a termination for convenience, the contract would require the contractors to return to the Government over $250 million of the unliquidated progress payments they currently hold.

C. Any Invocation Of State Secrets Would Not Affect The Loss Adjustment

The court of appeals vacated the Court's previous ruling that it would be "unfair" to apply a loss adjustment if the state secrets privilege deprived the contractors of an attempt to reduce the effect of the loss adjustment by proof of their superior knowledge claims. *See McDonnell V*, 37 Fed. Cl. at 281. As discussed above, we contend that the Court need not reach the issue of state secrets due to evidence precluding the contractors' ability to establish mandatory elements of their superior knowledge claim. We intend to present evidence of, among other things, the contractors' (a) refusal to heed the Navy's warnings regarding their weight estimate prior to award; (b) refusal to pursue opportunities to obtain access to classified information held by other defense contractors for cost reasons or fear of litigation over proprietary issues; and (c) contemporaneous conclusions that B-2 and F-117A data would not

have affected their contract proposal or execution of the FSD contract, all of which will preclude the contractors from establishing these elements. Finally, even if the contractors could establish the elements of their superior knowledge claim, "the passage of time and . . . possible intervening developments" would require a re-examination as to whether the risk of disclosure of state secrets would preclude adjudication of the contractors' superior knowledge claim. *See McDonnell*, 182 F.3d at 1330. Such a re-examination likely would indicate that the Court could decide all relevant issues without implicating the privileged evidence.

* * * *

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

PLAINTIFFS' RESPONSE TO "DEFENDANT'S STATEMENT OF ISSUES AND NOTICE OF PROBABLE TESTIFYING EXPERTS FOR TRIAL"

Pursuant to the Court's direction and the agreement of the parties, McDonnell Douglas Corporation and General Dynamics Corporation ("the contractors") respectfully file this response to the "Defendant's Statement of Issues And Notice of Probable Testifying Experts For Trial" (filed July 11, 2000) ("Govt. Statement"). The contractors set forth below their statement of issues responsive to the government's brief. While that brief is sufficient for the contractors to join issue with the government on various broad subjects, the government has not yet identified all of the specific factual grounds on which

it will try to justify the termination for default. Those allegations, whatever they are, will determine the scope of the trial and pretrial discovery. The government's brief is insufficient to focus the parties' trial preparation efforts. For the discovery and trial process to be efficient and fair, the government must identify all of the factual grounds on which it intends to rely, and must complete the process of identifying experts and providing their final reports. As explained further below, the contractors requested a meeting with the government in an effort to clarify these issues, and the contractors are still hopeful such a meeting will occur. In the meantime, the contractors provide this response to the government's brief, as well as the contractors' statement of the issues.

* * * *

H. The Default Termination Must Be Set Aside Because the Government Possessed Vital Superior Knowledge and It Failed to Take Any Action to Protect the Contractors from Their Lack of This Vital Knowledge.

With respect to the contractors' superior knowledge defense, the government attempts to make the same arguments this Court already has rejected. As this Court correctly ruled, the mere fact that the superior knowledge may be classified does not relieve the government of its superior knowledge duty. *See McDonnell Douglas Corp. v. United States*, 27 Fed. Cl. 204, 205-06 (1992) (quoting *J.A. Jones Constr. Co. v. United States*, 390 F.2d 886, 893 n.14

(Ct. Cl. 1968)). The Federal Circuit's opinion supports this Court's ruling. In answer to the government's argument that no such duty exists as a matter of law, the Federal Circuit necessarily rejected that argument by ruling that this Court was free on remand to adjudicate the merits of the contractors' superior knowledge defense (*if* circumstances have changed such that the superior knowledge issues can be litigated without jeopardizing national security). *See McDonnell Douglas*, 182 F.3d at 1329-30.

Moreover, this Court already rejected the government's arguments, *see* Govt. Statement at 18-20, that the contractors could not make out a prima facie defense of superior knowledge. *See McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 270, 281 (1996) ("At trial, plaintiffs would establish their superior knowledge claim."); Opinion and Order, at 2 (June 21, 1993) ("[P]laintiffs made an impressive showing that they can present a prima facie case under the existing discovery restrictions imposed by the defendant."). Accordingly, if the Court continues to conclude that the government's invocation of the state secrets privilege prevents trial of the contractors' superior knowledge defense, the Court must convert the termination for default into one for convenience. *See, e.g., Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1141 (5th Cir. 1992).

Furthermore, if the Court proceeds to trial on the superior knowledge issue, the contractors will prevail. The government possessed superior knowledge from other classified programs about weight, schedule, and cost that was essential to bidding on and to performing this contract. The government "was not free, if it was aware of the impending avalanche and knew that [the contractor] was not, to stand aside and let the bidder be overwhelmed without a warning." *J.A. Jones*, 390 F.2d at 888. But that is what the government did here. Prior to award, the government took *no* action to protect the contractors from their lack of this information. Indeed, the government took advantage of the contractors' lack of this vital knowledge and induced them to enter a fixed-price incentive contract with weight, schedule, and price terms that the government – based on its vastly superior knowledge – did not believe were achievable at the time of contract award.

I. Because the Sum Total of the A-12 Contractual Requirements Was Impossible to Perform, the Termination Must Be Converted to One for Convenience.

A contract is "impossible" if it is "absolutely impossible (in the sense of requiring performance beyond the state of the art)" or if it is commercially impracticable "'because of extreme and unreasonable difficulty, expense, injury or loss involved.'" *Foster Wheeler Corp. v. United States*, 513 F.2d 588, 594 (Ct. Cl. 1975) (emphasis omitted; quoting

Restatement of Contracts § 454). The evidence will establish that it was legally impossible to perform the sum total of the A-12 contract requirements, as well as certain individual requirements.[7] Under well-settled law, if a contract is impossible to perform, a contractor "is entitled to recover its costs of attempting to perform the contract," as long as it did not assume the risk of impossibility. *Foster Wheeler*, 513 F.2d at 594, 598.

In determining which party assumed the risk, the courts consider two factual questions: "(1) which party had the greater expertise in the subject matter of the contract? and (2) which party took the initiative in drawing up specifications and promoting a particular method or design?" *Foster Wheeler*, 513 F.2d at 598. The government assumed the risk of impossibility in this contract: the government initiated and drove the contract specifications, the government possessed the balance of the knowledge regarding the full-scale development of low observable air vehicles such as the A-12, and, as this Court has found, *see* Order (March 10, 1995), the government certified by law that the risks had been reduced to undertake this contract on a fixed-price basis.[8]

* * * *

[7] This Court already found that "the original predicted weight was unachievable." *McDonnell Douglas*, 35 Fed. Cl. at 373.

[8] There is no support in law or logic for the government's contention that the doctrine of impossibility does not apply to research and development contracts. *See* Govt. Statement at 20-21. The conclusion that the contractor assumed the risk in

J.A. Maurer, the case relied upon by the government for this contention, is simply a fact-specific application of the well-established legal principles for determining, case-by-case, which party assumed the risk. *See J.A. Maurer, Inc. v. United States*, 485 F.2d 588, 594-96 (Ct. Cl. 1973); *see also Foster Wheeler*, 513 F.2dat 601 (describing *J.A. Maurer* as a case in which the contractor "had expertise superior to the Government's, and that in some manner the initiative was wrested by the contractor from the Government's hands").

McDonnell Douglas v. U.S. No.: 91-1204C
August 10, 2000

Heritage Reporting Corporation

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IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORP. AND GENERAL DYNAMICS CORP., Plaintiff, v. THE UNITED STATES, Defendant.) Docket No. 91-1204C

Courtroom 4, Room 501
National Courts Building
717 Madison Place, N.W.
Washington, D C
Thursday
August 10th 2000

The parties met pursuant to the notice of the Court at 10:32 a.m.

BEFORE HONORABLE ROBERT H. HODGES, JR
Judge

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25

* * * *

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* * * *

MR. SNEE: Thank you. I would suggest at least one point of clarification and a couple other more substantive points. First of all, let me clarify this point right here. This other specifications issue. The heading is not meant to say, oh, there's some other pile of secret things that I didn't know about. This simply says they allege the government waived the weight specs. They allege the government waived the schedule specs. I've identified

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five things up here. My point is if they were to win waivers not completely dispositive, they would have to show that we waived the defects with propulsion, that we waived the defect with the structural framework and that we waived financial inability. So other specifications does not mean

there's some unidentified body out there. It just means
even if they could make a weight hearing, a weight waiver
even if they could make a schedule waiver. That doesnt
answer all the · with respect to other bases for default
So there s not some huge pile of unidentified stuff floating
out there.
The second quick point is about the experts stuff
The Plaintiffs say basically that they could live with this,
sort of this schedule, they could live with this date so
long as they don't have to do anything, so long as they
don't have to identify their affirmative defenses, their
experts, their defenses, their issues for which they bear
the burden of proof. Basically, what the Plaintiffs tell us
today is they're more than happy to go ahead and have a
trial, a portion of trial, in which apparently only certain
issues are going to be litigated, not their defenses to the
default and at some unknown at some unknown time in the

future, the government might find out what their defenses
are, might find out who the experts they intend to rely on,
and indeed, as Ms. Listrom said, they say very specifically

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in their paper, "furthermore, the contractors expect that
they may use experts on their affirmative defenses". I
believe Ms. Listrom just referred to that document. There
is nothing on those affirmative defenses, - experts on
waiver for superior knowledge or impossibility that have
anything to do with the governments case. And if we're
going to have a date that says, I've got to put up or shut
up with my story, then Ms. Listrom is right. What's good
for the goose is good for the gander. They have to have the
exact same date to put up or shut up with respect to their
experts. I believe they have them. I believe they choose
for tactical reasons not to name them, but I'm not going to
spend a lot of time exploring their motivations. All I'm

asking is that whatever those date be, they are the same for
both sides
The process which the Plaintiffs have suggested
today will not lead to final resolution of this court - of
this case in this court in the next calendar year. They're
talking about six months from November starting a trial on a
portion of the case and then at some other point apparently
the government might find out what their defenses are, might
get some opportunity to take discovery of their experts, and
then we'll have a second proceeding before we'd ever reach
any damages issue that remained in the case
So we believe, Your Honor, that that kind of

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construct in which we would bifurcate liability is quite
frankly, Your Honor, nonsense. The issues in this case
using impossibility or superior knowledge or waiver are
bound up exactly with the government's case on schedule on
propulsion, on all of those issues, and they cannot be

separated as conveniently as the Plaintiffs suggest
Last I would point out, Your Honor, there appears
to me to be a dichotomy in the Plaintiffs position. On the
one hand as the papers suggest and Ms. Listrom suggests
they have experts on the affirmative defenses. They just
dont want to name them now. On the other hand Mr. Potter
and to an extent Ms. Listrom, told us that everything in
the record is there already for them to win. They've
already got all the findings all the evidence in the record
that they need to win.
Quite frankly, I don't care which approach they
choose. I just want them to choose an approach and tell me
what it is. If they really believe that they have
everything they need to win this entire case on the record
then this is going to be an even shorter trial because I'm
going to put on my case, and they're going to have nothing
to put on. The case will be over. If, on the other hand
as Ms. Listrom says, well, they got 14 experts and they've

had some for a long time and they'd like they want some
opportunity some time later to take a second bite of the

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apple, well, then they'll have a different set of defenses.
And all I'm saying is literally, it is time to put up or
shut up. It is time to have a schedule. Both sides live
with that schedule, and you can resolve this case. I
believe in enforcement of that schedule. You can resolve
this case fully and fairly, allowing enough time for both
sides.
Those dates I told you earlier are aggressive.
They're just as aggressive for me. If Ms. Listrom comes in
with 14 expert witnesses like they did in 1996, I've got to
hustle just as fast as they do to get those expert reports
reviewed, turned around, get a deposition and get it out
So what I'm asking them to do is to agree to a burden that
is no greater burden than what they're asking me to do. And
that's why we believe the schedule that set dates for both

sides equally will lead to a schedule that will be can be
met. And on that note, without any objection, I would at
least like to leave you with a written copy of our schedule,
since we did not previously provide one to you, Your Honor.
Thank you.
THE COURT: Thank you. All right. Here's what
I'm going to do. I'm going to handle this differently from
the way I normally do in a case. And while I'm tempted Mr.
Potter, to take everything out of the case that I think I've
already ruled on, the opinion, whatever it means, I think

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does mean that the circuit wants everything in the record,
so I'm going to put everything in the record. And so that
it will be there when anyone wants to go to the Supreme
Court or wherever they want to go with it.
But that doesn't mean I'm not going to trim the
issues here. And if the Plaintiffs are willing to start in
May, it may mean that I can, after trimming the issues and
narrowing them, we can start in April, and

that might give
us enough time to finish according to my deadline, which is
to get the opinion out by August. That's my absolute
deadline, so that's what we all need to work toward. And it
may be that May or April is okay if we can focus it enough.
But what I want you to do is exchange contention
interrogatories. I want you to ask the government exactly
what you brought up here today, how are you going to prove
this. And then I want you, Mr. Snee, to do the same thing
to them. How are you going to establish your affirmative
defenses? Who's going to testify about it? What are they
going to say?
When this trial starts I want everyone to know
exactly what's going to happen just as though it were a play
that we rehearsed for months ahead of time. And we're going
to put it into the record, and I'll sit here and listen to
the witnesses and I'll judge their credibility and I'll make
findings of fact.

But I want you folks to know exactly what's going to happen, just as though they were lines in a play. And we do that by a series of contention interrogatories. And I'll issue an order to all this later. I'm thinking as I'm speaking, I'm not sure what all the details will be, but I would expect that these interrogatories will be exchanged on a rolling basis. In other words, in some case, Mr. Potter may say, well, I'm not sure how we're going to prove that yet, or I don't know what witness is going to establish that. I'll let you know. And then when you find out a month later, you let him know. And I want these to be back and forth on a continuing basis. The two that have here, as you've all heard, don't seem to satisfy anyone, and to some extent, they're ships passing in the night, so this process of rolling contention interrogatories will narrow that. You can say what do you mean by that, what do you mean by number 7, that's vague, be

more specific. And I'll referee that process. And then,
without imposing on your time, which will be taken up with
other things, I'll want to get together frequently to talk
about the status of these interrogatories and how things are
going. Appendix G, I dont care that much about, frankly.
But I think this is more helpful. It would be to me. So
there you are, and that's my plan, and I will try to put it
in a written form that makes some sense and issue it to you

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immediately. Yes?

MR. SNEE: Your Honor, may I be so bold as to make
just one other suggestion for consideration. It was a thing
we had talked about - and I had not raised with my
colleague - but we believe, Your Honor, and we spent a
little time looking at it, that there are a substantial
number of facts that the parties should be able to
stipulate, totally undisputed. And we have done this
successfully in the past in some instances. Not

so
successfully in other instances. And I think it tends to be
not so successful when each side tries to state it a certain
way or whatever, but that I still believe when you look at
that and we try to take a crack at that, there are just some
undisputed things which I think both sides would want for
completeness.
They're important enough to maybe be able to say
in closing argument or show a witness, but wanting to spend
witness time laying a foundation that a meeting was held on
a certain date and here's the memo that came from that
meeting. And so we would at least urge you to consider
that. We are certainly prepared as soon as we have a first
draft done we will send it to the Plaintiff saying - and
I'm talking about, you know, about kind of a stipulation of
fact. I don't envision, like our position paper, you know a
20, 25-page thing with attachments to it and the basic

framework. But I, we are very please to do that. I only raise it now because you're issuing the order. I haven't had a chance to talk to them about it but we're happy to do that and we're happy to take the first whack at it and send it out the door as soon as we can and ask that you consider that as you draft this order.

THE COURT: I have no idea why I left that out. That's the number one thing I wanted cover. Stipulate as much as we can. And I'd like for you to stipulate the expertise of your expert witnesses. I dont want to go through that routine on the stand. I don't care where he went to school. I just want to get to his testimony. And stipulate the authenticity of documents. That's usually not a problem anyway. Most of them are government documents So I don't want to go through the routine of saying is this your signature, was it in your possession and all that. We dont need to gum up the works with that sort of testimony. So anything that any of you can

think of as
we go along, such as stipulating the key facts, please bring
them up and I'll add it to the list. Thank you very much.
MR. POTTER: Your Honor, if I might. I know its
unusual to file with the Court, but would it be helpful
here, in order to keep you advised of what's going on if we
would actually send you courtesy copies.
THE COURT: Yes. I meant to -

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MR. POTTER: Not actually file in the clerk's
office but we send you a copy and the answer, because I
think that might be helpful.
THE COURT: That's what I meant by it. I was
being a little obtuse. That's what I meant by referring
I do expect to see copies of these as they come through.
Thank you very much. I appreciate you being here

* * * *

McDonnell Douglas v. U.S. No.: 91-1204C
December 19, 2000

Heritage Reporting Corporation

Page 1 to Page 76

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IN THE UNITED STATES COURT OF FEDERAL CLAIMS

MCDONNELL DOUGLAS CORP.
Plaintiff,
v.
THE UNITED STATES,
Defendant.

) Docket No. 91-1204C

Courtroom 7, Room 508
National Courts Building
717 Madison Place N.W.
Washington, D.C.
Tuesday
December 19, 2000

The parties met pursuant to the notice of the Judge at 2:06 p.m.

BEFORE HONORABLE ROBERT H. HODGES, JR.
Judge

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* * * *

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THE COURT The Secretary has gotten back from Europe and he or she is sitting there today, as we speak looking at some information that none of us has officially. You don't have plaintiffs don't have I don't know whether I have it or not. All right. What you're saying is let's assume that the Secretary is not going to permit this information into the case and you said there s not that much. But the answer is yes that's your approach, right? You re saying, yes, we will proceed as though this information is out of the case.

MR SNEE No, what I think I'm trying to say is we should proceed with respect to expert reports on the schedule we have, regardless of whether this information is in or out of the case, because if it's in the case, if some new information becomes available, it's no different than the fact that I'm still waiting to get some GE documents or I'm waiting to get some structural drawings

that I need or
19 I'm waiting to get some more financial information that I
20 need to produce those reports. If that's the standard, that
21 nobody can produce an expert report until every single piece
22 of discovery requested has been made available and turned
23 over, then we're never going to get expert reports.
24 Conversely, if the privilege is invoked, then, in fact,
25 there's absolutely been no impact whatsoever, because there

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1 is no basis upon which any expert could potentially change
2 his opinion.
3 So, what I'm really urging is that the plaintiffs
4 simply do what we have done, give us their reports as they
5 exist today, give us their work papers, give us their – as
6 it exists today, so we can prepare to study, to begin to
7 depose, to know how to do that I may not depose them
8 today, but I certainly am entitled to start reading those
9 reports and reading those work papers, just like they are
10 reading ours.

On a parallel track, the Secretary of the agency concerned, I believe, is going to make a decision in the very near future probably before I can depose anybody, as to whether or not he would invoke the state secrets privilege with respect to this issue at issue, and whether he does or doesn't may have an impact on the case. By the time that potential impact gets brief, gets argued, and I get to depose Mr. Mar, Mr. Rooney, and Mr. whoever, to make a record of that, in our view, there's no way that a state secrets impact could effect their ability to render an opinion. It's going to be May. It's going to April. And so all we're asking for is give us the reports, give us the work papers you have right now. And I will accept Mr. Churchill at his word, that we will take January 31st as the date for their claims report. I'll live

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with that. It's a week after what we're offering them. That's a quid pro quo. Now, all I want is date certain

between now and then that I'm going to get the three remaining reports from all those materials that are available. And if they're not time state secrets the privilege is asserted, the plaintiffs can argue whatever brief they want, but those two matters should proceed on a parallel track. That's the only way we're going to start on May 1, finish by August 30th, have a complete record and have no surprises. And so, we're not asking for anything more than what we have already given them.

THE COURT Now, you've issued your expert reports minus the GE information, is that right?

MR SNEE I'm sorry?

THE COURT The GE information?

MR SNEE We have outstanding GE information -- GE documents. We have outstanding some structural drawings from the plaintiffs, things that relate to the actual structure of the aircraft. And we have outstanding – I'm not sure if we have outstanding further financial discovery. We've gotten production just on Friday and I

think at least
22 one of the plaintiff represents it's complete although we
23 haven't been able to go through the nine boxes.
24 So, there are at least three areas where I know
25 there is factual information outstanding I have produced

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1 one of those – two of the reports already relating to that.
2 We are prepared to produce –
3 MR POTTER No. You haven't furnished the
4 structural report –
5 MR SNEE No.
6 MR POTTER – or financial report.
7 MR SNEE I said, the two propulsion reports.
8 We're permitted to produce the structural report on
9 Thursday. And if the rule is, you don't have to produce
10 anymore expert reports until you get every piece of paper
11 then, obviously, Your Honor, we shouldn't be obligated to
12 produce our structural report on Thursday, while we still
13 have these drawings outstanding.
14 I was committed to produce the financial expert
15 report on the 22nd, four weeks from now, based on the fact
16 that we think we can get through these last nine boxes.

THE COURT That argument has a superficial appeal of parallelism, that somehow it doesn't seem quite the same to be waiting for information on a different subject matter, to file a different expert report, as it does to be waiting for information that is central to that whole case.

MR SNEE I guess, Your Honor, maybe we kind of diverged. Other than the plaintiffs' assertion that some information out there is central to their whole case, there's no – nothing in the record to establish that, in

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fact, it is essential to their case. So, until I get a report until I can depose them and say here's what my analysis is, we have no basis on which to make that assertion.

We know, for example, that the plaintiffs in response to contention interrogatories have dramatically altered their 'superior knowledge' claim. Let me tell you what they say in the contention interrogatory. They say

that their claim for superior knowledge is that the government failed to share information about schedule, information about cost, and information about weight estimation techniques. Those allegations that they make in their contention interrogatories comes exclusively from Nothrop's competing proposal on the ATA program. So after 500,000 pages of B2 documents having been made available, copied and delivered to them, their superior knowledge claim boils down to – stealth airplanes take a long time to build, they're really expensive, and you've got to be careful how you estimate weight. I can absolutely assure you that you can fully and fairly try all three of those claims on probably unclassified information, let alone just A12 classified information.

So I guess maybe where we diverge is I categorically reject the notion that because the plaintiff's

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counsel asserts that it's critical to their report, that

that somehow relieves them of the obligation to produce the report. Let's see the report, let's see the work papers, and come back here in 10 or 15 days, if necessary, and then decide whether or not that's somehow critical. But, I believe, in fact, is occurring, Your Honor, is what that footnote suggests, that although they've been working hard, they simply haven't gotten done yet and they prefer not to produce those reports.

But, quite frankly, Your Honor, that's not – I may be crude about it, but that's not my problem. I've met our schedule of commitments and I want to prepare to meet the reports that they are saying they're going to rely upon. And the only way to minimize that damage is to send us now what they have and commit to a date certain by which they would complete those reports, within the next two or three weeks.

* * * *

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DEFENDANT'S NOTICE OF AN *EX PARTE* FILING IN CONNECTION WITH PLAINTIFFS' 29th AND 30th SETS OF DISCOVERY REQUESTS

Defendant provides notice that it has lodged with the designated Court Security Officers for the United States Air Force an *ex parte* filing in connection with Plaintiffs' 29th and 30th sets of discovery requests.

On September 1, 2000, plaintiffs served their 29th Set of Interrogatories and 31th Request for Production of Documents and on October 26, 2000, plaintiffs served their 30th Set of Interrogatories and 32nd Request for Production of Documents (collectively "plaintiffs' 29th and 30th sets of discovery"). Both sets of discovery requests contain

certain requests for information that the United States Air Force has determined not to release and over which the Secretary of the Air Force has invoked the state and military secrets privilege. Attached to this notice of an *ex parte* filing is a copy of an unclassified declaration by the Secretary of the Air Force, dated January 8, 2001, invoking the privilege and explaining his rationale for so doing. Attached to the *ex parte* filing itself is a classified declaration by the Secretary of the Air Force, also dated January 8, 2001, repeating the invocation and further explaining his rationale.

Given that the *ex parte* filing and the classified declaration of the Secretary of the Air Force contain highly-classified information, they cannot be stored or maintained in the existing filing facilities of the office of the Clerk of Court. Accordingly, the *ex parte* filing and attached classified declaration of the Secretary of the Air Force have been lodged for safekeeping with the designated Court Security Officers for the United States Air Force, and this notice is being filed in public record. The *ex parte* filing and the classified declaration are maintained by the Air Force at the following location:

Office of Director
& Security Oversight
SAF/AAZ
Room 5D972
1720 Air Force Pentagon
Washington, D.C 20330-1720

and are available to the Court, at its request, for review. The primary Court Security Officer for the Air Force is Mr. John Keller, (202) 305-7700; the alternate Court Security Officer for the Air Force is Mr. Dennis Morgan, (703) 558-2135.

Respectfully submitted,

STUART E. SCHIFFER
Deputy Assistant Attorney General

/s/DAVID M. COHEN/BG SNEE
DAVID M. COHEN
Director

/s/ BRYANT G. SNEE
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February 7, 2001

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DECLARATION OF THE SECRETARY OF THE AIR FORCE F. WHITTEN PETERS

I, F. Whitten Peters, declare:

1. I am the Secretary of the Air Force. As such, I am currently the head of the Department of the Air Force. I am responsible for, and have the authority necessary to conduct, all affairs of the Department of the Air Force as specified in Section 8013, Title 10, U.S. Code. Subject to the authority, direction and control of the Secretary of Defense, I am also presently responsible for the formulation of policies and programs by the Department of the Air Force that are fully consistent with national security objectives and policies established by the President and the Secretary of Defense.

2. In my capacity as chief executive officer of the Air Force, I possess original classification authority and am authorized by the President under Executive Order 12958 to determine the proper classification of information.

3. The purpose of this public declaration is to invoke the military and state secrets privilege in order to protect the national security of the United States. This declaration addresses the same matters that were the subject of the 30 March 1993 declarations of then-Acting Secretary of the Air Force Michael B. Donley invoking the military and state secrets privilege. Because a more detailed public description of certain matters for the record is not possible, I am also submitting *in camera* a classified declaration to the Court, which provides a further explanation of this invocation of the military and state secrets privilege.

4. The statements in this declaration are based upon my personal review and consideration of these matters. Specifically, among other things, I have considered the 30 March 1993 classified and unclassified Declarations of then-Acting Secretary of the Air Force Michael B. Donley invoking the military and state secrets privilege, the 22 July 1993 Declaration of then-Acting Secretary of the Air Force Merrill A. McPeak, and the 30 April 1993 order of the Court of Appeals for the Federal Circuit holding that "here the circumstances were 'appropriate' for assertion of the Military and State Secrets Privilege" by Acting Secretary Donley, and I have reviewed the

nature of the information described in more detail in my classified declaration.

A. *General Classification Procedures and Restrictions Upon Access To National Security Information*

5. Generally, classification of information within the Department of Defense is done in accordance with Executive Order ("E.O.") 12958, which prescribes a uniform system for classifying, declassifying, and safeguarding national security information. Executive Order 12958 (April 17, 1995), 3 C.F.R. 333 (1995), 60 Fed. Reg. 19825, as amended by E.0.12972 (September 18, 1995), 3 C.F.R. 407 (1995), 60 Fed. Reg. 48863 and E.O. 13142, (November 19, 1999), 3 C.F.R. 236 (1999), 64 Fed. Reg. 66089; and Presidential Orders of October 13, 1995, 60 Fed. Reg. 53845; February 27, 1996, 61 Fed. Reg. 7977; and February 26, 1997, 62 Fed, Reg. 9349. E.O. 12958 authorizes three levels of classified information: "Top Secret," "Secret," and "Confidential."

6. Pursuant to Department of Defense ("DoD") 5200.1-R, January 14, 1997, it is the policy of the Department of Defense to use security classification categories of E.O. 12958. In addition, however, the Deputy Secretary of Defense upon a recommendation from the DoD component involved may establish a program as a "special access program" when absolutely necessary to protect the Nation's most sensitive and critical information or

when required by statute. E.O. 12958; DoD Directive O-5205.7, January 13,1997.

7. A DoD program employing enhanced security measures exceeding those normally required by DoD 5200.1-R for information at the same classification level shall be established, approved, and managed as a "special access program." The "special access" designation is reserved for particularly sensitive classified programs in order to control the access and distribution of information pertaining to these special access programs.

8. An individual must possess a security clearance of secret or top secret as a prerequisite for access to a special access program. Possession of a security clearance is only the first step toward approval for access to a special access program. These programs are characterized in part by an additional adjudication, to a more stringent standard than the adjudication for a security clearance. *See* DoD 5200.2-R, 52 Fed. Reg. 11,219 (1987) (codified at 32 C.F.R § 154) (outlining security review of personnel in special access programs).

9. Special access programs also impose "need to know" and access controls beyond those normally required by DoD regulations for access to confidential, secret, and top secret information. Access to information within a special access program is granted only to those persons who are essential to the successful completion of the program, and who meet all stipulated security requirements. Other more stringent security measures in effect in

special access programs are enhanced physical, technical, communications, computer, operations, and information security.

10. Special access programs may be acknowledged (overt) or unacknowledged (covert) in nature. The mere existence of an unacknowledged program is classified within the boundaries of the special access program. That is, one must be approved for access before one may know that the program exists at all.

11. A further aspect of special access programs is that they are "compartmented." That is, the information in the program is, in effect, walled off from other classified information and programs. For example, it is not uncommon that individuals, either Government or contractor personnel, may work in a secure facility that contains more than one special access program. An individual may have access to one special access program while his colleagues have access to different special access programs. Despite the fact that the individuals are professional colleagues, that they possess the requisite security clearances, and they work in the same secure facility, such individuals are still prohibited, absent being given access to another program, to share special access information across program boundaries. The purpose of this requirement is that in the event of a breach of security the potential damage is limited to that one special access program. In effect, the "compartmented" nature of a special access program

works as a damage control brake, in the event of an unauthorized disclosure.

B. *The Information at Issue and the National Security Interests at Stake*

12. The specific reasons why discrete disclosures would endanger national security are necessarily explained in more detail in the accompanying classified declaration. Generally, however, the United States is the world leader in the production and operation of low observable technology weapons and aircraft. Low observable weapons systems and aircraft have been used in combat, without the loss of United States life. I believe that no foreign country presently has either the comparable capability to build low observable aircraft or the capability to develop robust, credible countermeasures to this technology. The United States has a very limited capability to counter this technology, should it be developed and used against us by a foreign country. Accordingly, the United States protects its low observable capabilities within Special Access Required channels because inadvertent, unauthorized disclosure of the low observable technology information that is described in more detail in my classified declaration could be expected to cause exceptionally grave damage to national security.

13. The information at issue cannot be commented upon further in a public declaration, and my determinations in that regard are described in more detail in the classified declaration.

C. *My Determinations Regarding National Security And The Military and State Secrets Privilege*

14. The Air Force cannot confirm or deny the existence of the information sought by plaintiffs.

15. Even if the parties and Court attempted to take all conceivable precautions, I believe that there is a substantial risk that national security would be threatened by disclosure of these matters, for purposes of this litigation. Accordingly, I view my responsibility to protect the national security as requiring that I invoke the extraordinary measure of asserting the military and state secrets privilege.

16. I have personally determined that the privilege claims that I now assert in this declaration are appropriate under the circumstances.

17. For these reasons, and the reasons explained in more detail in the accompanying classified declaration, I invoke the military and state secrets privilege for the information sought by plaintiffs.

18. This present assertion is limited to the matters that are the subject of the 30 March 1993 declarations of then-Acting Secretary of the Air Force Michael B. Donley and my classified declaration.

19. I declare under penalty of perjury that the foregoing is true and correct.

/s/ F. WHITTEN PETERS
F. WHITTEN PETERS
Secretary of the Air Force

Executed this 8th day of January, 2001.

CERTIFICATE OF SERVICE

I certify under penalty of perjury that on February 7, 2001, I caused to be served copies of "DEFENDANT'S NOTICE OF AN *EX PARTE* FILING IN CONNECTION WITH PLAINTIFFS' 29th AND 30th SETS OF DISCOVERY REQUESTS" by facsimile transmission and hand delivery addressed as follows:

Caryl A. Potter, III, Esq.
SONNENSCHEIN
NATH & ROSENTHAL
1301 K Street, N.W.
#600, East Tower
Washington, D.C. 20005

and by facsimile transmission and overnight courier as follows:

Linda L. Listrom, Esq.
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Chicago, ILL 60611

/s/

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

No. 91-1204C

(Filed: March 1, 2001)

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	THIS OPINION AND ORDER WILL NOT BE PUBLISHED.
v.	)	
THE UNITED STATES OF AMERICA,	)	
Defendant.	)	

Caryl A. Potter, III Sonnenschein Nath & Rosenthal, Washington, D.C., for plaintiff McDonnell Douglas Corporation; *Linda L. Listrom*, Jenner & Block, Chicago, Illinois, for plaintiff General Dynamics.

Bryant G. Snee and *Patricia M. McCarthy*, United States Department of Justice, Washington, D.C., for defendant.

OPINION AND ORDER

HODGES, Judge.

INTRODUCTION

We ruled in December 1996 that certain issues related to superior knowledge could not be tried because the resulting threat to national security would not permit it. This determination was based in part on the Government's invocation of the state secrets doctrine and partly on "a series of security breaches and discovery abuses . . . ." *McDonnell Douglas Corp. v. United States*, 182 F.3d 1319, 1329 (Fed. Cir. 1999). The Federal Circuit asked us to reconsider that Order, but the circumstances that prompted the ruling still pertain. Therefore, we must reaffirm the December 13, 1996 Opinion and Order for the reasons stated therein.

DISCUSSION

The Federal Circuit's opinion speculated that some of the restrictions on superior knowledge issues would be removed by now, "[b]ecause of the passage of time and of possible intervening developments . . . ." *Id.* at 1330. The Circuit questioned "whether the risk of disclosure of state secrets will preclude adjudication, on remand, of Contractors' superior knowledge claim, and the issues of loss adjustment and reasonable profit." *Id.* Since then, the parties have been conducting discovery and exchanging contention interrogatories in preparation for a trial to begin on May 1. In the course of that discovery,

plaintiffs have issued several interrogatories that have prompted the United States to invoke again the military and states secrets doctrines to protect information that is necessary to resolution of these issues.

We reviewed the declaration by The Secretary of the Air Force, F. Whitten Peters, and determined that it comports with the legal requirements for invoking the state secrets doctrine as set forth by the Federal Circuit. An unclassified version of the Secretary's declaration is attached to this Order and incorporated herein by reference. We have also reviewed the classified version of Secretary Peters' declaration, and we are satisfied that superior knowledge issues in this case cannot be litigated safely. This determination is based on that declaration and the warnings described therein, as well as those of previous government officials.[1] We know from recent briefings that all of these warnings still apply.

[1] *See also* McPeak Declaration at 2-3 (July 22,1993) ("I have concluded that continued inquiry into what is known as plaintiffs' 'superior knowledge' claims would necessarily require examination and use of information that cannot be disclosed in this litigation."); *see also* Donley Declaration at 5-6 (March 30, 1993) ("[i]nadvertent, unauthorized disclosure of the information that is described in more detail in my *in camera* declaration could severely jeopardize national security."); *see also* Rice Declaration at 4-5 (November 20,1992) ("The unauthorized disclosure of the national security information at issue reasonably could be expected to cause extremely grave damage to the national security . . . . this will weaken our country's ability to defend itself and could place at risk our aircraft and the lives of the crews of those aircraft.")

The reasons for removing the superior knowledge issues from the case for trial beginning in May, along with the legal bases for this determination are set out in full at *McDonnell Douglas v. United States*, 37 Fed. Cl. 270 (1996). All of the reasons established by that December 1996 opinion persist. The Appendix to which we referred in earlier orders remains classified under seal at the Pentagon. The reviewing court may wish to address those matters should it have the occasion to reach this issue again.

CONCLUSION

Issues involving superior knowledge, profits, and loss adjustment will not be litigated further in this court. Defendant may not obtain a lost adjustment pursuant to FAR 49.203, and plaintiffs may not obtain profits pursuant to FAR 49.202. Counsel will take this ruling into account in considering their recommendations for the scope of trial to begin in May.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

PLAINTIFFS' STATEMENT OF ISSUES AND LEGAL STANDARDS FOR TRIAL

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IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

PLAINTIFFS' STATEMENT OF ISSUES AND LEGAL STANDARDS FOR TRIAL

This Court asked the parties to brief what "the issues in this trial are going to be and the standards that I should use in light of the Circuit's decision to resolve this case." *See* Hearing Tr. at 5 (Nov. 16, 2000). In response to this request, plaintiffs McDonnell Douglas Corporation and General Dynamics Corporation ("the contractors") respectfully file this brief.[1] The brief first addresses the scope of the mandate from the Court of Appeals and then addresses the issues for trial, as well as the

[1] The government already filed its brief on these issues. *See* Def's Brief Regarding Issues to Be Addressed and the Appropriate Trial Standards to be Applied at the May 1, 2001 Default Trial (filed Feb. 12, 2001) (hereinafter "Gov't Br.").

legal standards that govern them, regarding whether the termination for default is justified. With respect to the amount of the contractors' termination for convenience recovery, there are no issues to litigate because, as explained below, this Court's undisturbed rulings, including its Order of March 1, 2001, establish the amount of the contractors' recovery.

SUMMARY OF ARGUMENT

During the Critical Design Review, the Navy thoroughly reviewed all aspects of the A-12 aircraft. At the conclusion of that review, Admiral Lockard, the Navy's chief technical officer who had the final authority in the A-12 contract for all technical issues, declared: "Technical resolution on the airplane has been reached." Minutes of Design Review Board III, Part 2, dated Oct. 22, 1990, at 57 (admitted ex. 160) (attached as Tab B). Nevertheless, at the upcoming trial, the government seeks to hold a new Critical Design Review, presented by its litigation experts, with this Court sitting in the role of Admiral Lockard. The government cannot sustain its termination for default on that kind of evidence.

The Federal Circuit remanded for this Court to determine whether the government could justify its termination for failure to make progress under the general legal principles that govern such trials. Because the termination was one for an alleged failure to make progress, the Government can now rely only on the two grounds that were actually identified by Admiral Morris in the cure notice. Accordingly, the only possible grounds to justify the

default are: (1) the original weight specification and (2) the contractors' alleged inability to manufacture parts in time to meet the schedule. But as established by this Court's prior findings of fact, which were not disturbed by the Federal Circuit's decision, the government waived the original weight specification. Furthermore, the government simply will be unable to establish that the schedule it unilaterally imposed can be used to justify the default termination. Apparently recognizing these problems with its failure to make progress case, the government seeks to re-try its claim that these two major defense contractors allegedly repudiated this contract. But that claim has been finally, and correctly, decided against the government.

Even if the government could prove which it cannot that the contractors were materially failing to make progress toward an enforceable, unwaived contract requirement for which the government provided a proper cure notice, the contractors have affirmative defenses of superior knowledge and impossibility that each would independently excuse any noncompliance with the original contract requirements or any other alleged basis of default. But this Court recently ruled that "[i]ssues involving superior knowledge, profits, and loss adjustment will not be litigated further in this court." Order at 3 (Mar. 1, 2001). The Court's ruling correctly resolved the effect of the government's invocation of the state secrets privilege on the calculation of the contractors' termination for convenience recovery. *See id.* (incorporating *McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 270 (1996)). But the removal of

the superior knowledge issues from the case also will affect the ability of the contractors to complete discovery and to fully try their affirmative defenses of superior knowledge and impossibility, as well as the related defense of excusable delay.

In light of the government's invocation, as well as this Court's ruling, the contractors respectfully suggest that the Court stay at this time discovery and litigation on the contractors' defenses of superior knowledge, impossibility, and excusable delay. *See* Order at 3 (March 1, 2001) (requesting that the parties "take this ruling into account in considering their recommendations for the scope of trial to begin in May"). If, after the May 1 trial, the government has failed as it will to prove that the contractors were materially failing to make progress toward an enforceable, unwaived contract requirement for which the government provided a proper cure notice, the Court may never need to litigate the contractors' superior knowledge and impossibility defenses or decide the effect of the government's invocation of the state secrets privilege over evidence highly relevant to the contractors' ability to defend themselves against the government's termination for default claim.

Finally, if the Court once again converts the default termination to one for convenience as it should then, under this Court's undisturbed rulings (including its March 1, 2001 Order), there are no issues to litigate with respect to the amount of the contractors' termination for convenience recovery. Under this Court's rulings, the contractors are

entitled to recover the costs they reasonably incurred performing this contract, up to the amount of funding available at termination, plus interest. That amount is $1,200,132,820, plus interest on that sum from June 26, 1991, until paid. *See McDonnell Douglas Corp. v. United States*, 40 Fed. Cl. 529, 555-56 (1998). The Court should re-enter judgment for the contractors in that amount.

* * * *

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

----------X

MCDONNELL DOUGLAS CORP. and
GENERAL DYNAMICS CORP.

Plaintiffs,

v. No. 91-1204C
JUDGE HODGES

UNITED STATES DEPARTMENT
OF JUSTICE

Defendants.

----------X

Thursday, March 8, 2001
Washington, DC

A hearing in the above-captioned matter was held on Thursday, March 8, 2001 commencing at 10:50 a.m., in the Court of Federal Claims, 717 Madison Place, Washington, DC before

JUDGE HODGES

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* * * *

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* * * *

13 MS. LISTROM: Since portions of our brief

were up
there on the screen and referred to, I d like to explain
what our position is on superior knowledge, impossibility
and excusable delay. And, then I want to circle back to the
TASC issue which is what I started with. As Your Honor may
recall, the contractors have asserted two different defenses
to the imposition of a loss adjustment. One of them is
superior knowledge, a defense which Your Honor is familiar
with. The other is impossibility, a defense that you re
also already familiar with. Impossibility has two
components or two requirements. In order to prove up an
impossibility defense, the contractors have to prove that
they were being asked to do something that was beyond the

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state of the art and then they also have to prove that the
government had the balance of knowledge about the issue,
that the government knew more than the contractors did,
i.e., superior knowledge.

So, the superior knowledge is an aspect of impossibility and that s why we tend to treat the two of them together. They are very closely related because both the superior knowledge defense to a loss adjustment and the impossibility defense to a loss adjustment will inevitably get into proof about the superior knowledge question. The difficulty that has arisen and we have not had an opportunity to brief this issue to Your Honor, is that once you get past quantum and go back to the liability side of the case there, too, we have asserted some affirmative defenses. Superior knowledge and impossibility are two of our affirmative defenses. We also have a third affirmative defense which Mr. Snee referred to which is excusable delay,

And, I think it s pretty clear just from the snippets of our brief that Mr. Snee put up on the overhead projector, that excusable delay is based upon superior knowledge. So, we have three different defenses on the liability side of the

case, all of which, implication superior knowledge. Our superior knowledge defense, our impossibility defense and our excusable delay defense. Now, the question is what do we do about those

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defenses for the upcoming May 1 trial date in light of Your Honor s ruling on Quantum and your indication that you don t want us litigating superior knowledge. We believe that there is a good legal argument to be made that the government cannot hold the contractors in default and cause a forfeiture of a significant amount of money to the contractors while at the same time, depriving them through invocation of the state secrets privilege of information that they need to litigate these three defenses of superior knowledge, impossibility and excusable delay. We believe that an argument could be made that this case is over based on the ruling that you made last week because as a matter of law, they cannot pursue a default while at

the same time
14 invoking the state secrets privilege.
15 Now, we could take that position but I think
16 there's one thing that everybody sitting in this room today
17 agrees with, and that is we want to have a trial. And, you
18 want to have a trial on May 1 and we want to have a trial on
19 May 1 because we believe that we can defeat the government's
20 default or failure to make progress case without resorting
21 to our affirmative defenses of impossibility, superior
22 knowledge and excusable delay. We believe, as we've
23 indicated to you before and you've already seen a lot of
24 this evidence in count 17, the Navy was satisfied with the
25 progress that the contractors were making to the extent that

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1 there were some specifications that were not going to be
2 complied with or the plane was behind schedule, the Navy
3 waived all of that. We believe that we can prevail without
4 those affirmative defenses.
5 So, what we think makes sense here is to

go to
trial on May 1, let the government put on it's default case,
we will put on our defense to the default case without using
those affirmative defenses. Because we understand, based on
Your Honor s order, that you have real security concerns,
legitimate security concerns if the parties continue to try
and litigate the superior knowledge issue. So, let s go to
trial on May 1. We'll be here. We're going to put on a
defense. We believe that we can defeat the government's
case without getting into these defenses. And, that s why
we suggest that you stay all further and we understand
your order, frankly, as staying all further discovery and
litigation on these issues both as they relate to quantum
but also as they relate to liability.
Now, if we're wrong, and if Your Honor were to
find much to our surprise that the contractors were failing
to make progress, then we will want to take up this issue
with you again of superior knowledge,

impossibility, etc.
But, at that point what we believe it'll be is a legal
argument that the government can t default us while at the
same time withholding information from us that we need to

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make out a defense. I don't believe we'll ever get to that
day. But, if we do, I think the argument that we're going
to be left with is basically a legal argument which we'll be
prepared to make at that time.
So, that's the proposal that we lay out in the
brief that we filed last week. I think it's an effort to
accommodate, to take Your Honor's ruling which you issued on
state secrets last week and imprint that on the liability
case and figure out how we're going to proceed on the
liability case in light of Your Honor's ruling.
JUDGE: I don't think this is any different from
what we were planning. In other words, the government puts
its case on first. It has the burden. And; then maybe

you'll file one of those motions like the government always files directed at judgment and effect. I can't remember the rule number. And, then you put on your case your affirmative defenses.

MS. LISTROM: Exactly. Except that we will not be providing up affirmative defenses of superior knowledge and impossibility under our proposal.

JUDGE: Well, you can't put up superior knowledge. Now, impossibility I don't know why you couldn't put that up if you wanted to. I mean you can't use that element of impossibility but.

MS. LISTROM: Well, we could prove up -- there are

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two requirements to prove impossibility. We have to prove both that the specifications were beyond the state of the art and that the government had greater knowledge or superior knowledge. We have to prove both of those things.

JUDGE: There is no way we can get to that.

MS. LISTROM: There is no way we can

prove the
second thing so we could put on some evidence directed to
the first requirement. But, we're going to have a failure
of proof on our affirmative defense --
JUDGE: Well, it may be we'd have to have an
argument at that point than we've all wondered about for
years which is who pays when you invoke those state secrets
act.
MS. LISTROM: My guess is we're never going to
have to have that argument because we believe we're going to
be ready for trial on May 1, not withstanding some anxiety
that I've expressed to you in the past, we're going to be
ready. And, we believe that we can defeat this case without
getting into this sensitive information that you really
don't want us to get into. Now, I'll go ahead and yield to
Mr. Potter who I know is most anxious to speak.

* * * *

No. 91-1204C
(JUDGE HODGES)

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION
AND GENERAL DYNAMICS CORPORATION,

Plaintiffs,

V.

THE UNITED STATES,

Defendant.

DEFENDANT'S BRIEF REGARDING EFFECT OF STATE SECRETS AND MOTION FOR RECONSIDERATION

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Dated: March 28, 2001 Attorneys for Defendant

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IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DEFENDANT'S BRIEF REGARDING EFFECT OF STATE SECRETS AND MOTION FOR RECONSIDERATION

Pursuant to the Court's orders dated March 1 and 15, 2001, defendant, the United States, submits the following brief regarding the effect of the United States Air Force's invocation of the state secrets privilege upon this litigation, and it respectfully seeks reconsideration of the Court's order dated March 1, 2001 (the "March 1 order"). In addition, pursuant to the Court's March 15 order, today we file separately "Defendant's Reply Brief to Plaintiffs' Statement of Issues and Legal Standards for Trial," which constitutes our reply to plaintiffs' brief regarding issues other than those concerning state secrets and the effect of the March 1 order.

Below, we demonstrate that the March 1 order, which re-adopts the rationale of the Court's December 1996 damages opinion, *McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 270 (1996), and removes the issues of superior knowledge, loss adjustment, and profit from the entire trial, suffers from a number of fatal infirmities.

Foremost among our procedural concerns is the absence of any evidence in the record that links plaintiffs' current superior knowledge claim -- based entirely upon the A-12 FSED proposal submitted by Northrop Corporation -- to the state secrets and security concerns addressed in the Court's March 1 order and December 1996 damages opinion. There currently is no nexus between the evidentiary record of this case and the Court's ruling; thus, there is no evidentiary basis to support the Court's conclusion that the plaintiffs' current superior knowledge claim cannot be tried without creating the possibility of a disclosure of state secrets. We respectfully submit that a complete evidentiary record is a prerequisite for the Court's final determination as to the effect of a claim and an assertion of the state secrets privilege.

From a substantive standpoint, the United States maintains that plaintiffs' superior knowledge claim can be tried completely and safely. The post-remand clarification of plaintiffs' superior knowledge claim has rendered moot the rationale of the December 1996 damages opinion, which the March 1 order re-adopts. Since remand, the Court's

contention interrogatory process has exposed the superior knowledge claim's contained scope, which is far narrower than it appeared when the Court issued its December 1996 damages opinion. Because plaintiffs now admit that their superior knowledge claim rests exclusively upon the contents of their competitor's proposal for the A-12 contract, the Court can decide fully that claim based strictly upon unclassified and classified A-12 information. No state secret-related information could possibly aid plaintiffs' establishment of their superior knowledge claim in its current incarnation. This is precisely the type of "intervening development" that the court of appeals urged the Court to consider. Further, even if the scope of plaintiffs' superior knowledge claim were as broad as it appeared in 1996, the March 1 order does not apply the traditional legal rule as to the effect of the state secrets privilege, which is simply to remove the covered evidence from the case. The traditional legal rule requires the Court to decide all issues, including superior knowledge, profit, and loss adjustment, in the absence of the privileged evidence. No precedent permits a court to "sprea[d] the consequences" of an invocation of the state secrets privilege.

Finally, even though the Court's "no profits, no loss" rationale appears to have been adopted as an equitable matter, its ultimate effect is plainly inequitable. We believe that plaintiffs will be unable meet their burden to excuse their manifest default at trial. However, if the Court were to convert the default termination to one for convenience, the March 1 order's removal of the Government's

contractual right to apply a $1.5 billion loss adjustment -- *five times* the amount of plaintiffs' removed theoretical claim for profit -- would be extraordinarily punitive. In its December 1996 damages opinion, the Court concluded that it could not decide plaintiffs' requests for equitable adjustment ("REAs") that are based upon a claim of superior knowledge because, at the time, it appeared they were closely connected to state secrets-related information. The Court reasoned it would be a "sham" to apply the loss adjustment if plaintiffs were unable to defend against the loss adjustment with proof of all of their REAs. Thus, the Court decided that the Government's claim for a loss adjustment and plaintiffs' REAs and claim for a profit could not be tried. After removing loss adjustment, REAs, and profit from the damages case in 1996, the Court decided that plaintiffs were entitled to a judgment for all incurred costs. However, the consequences of the December 1996 damages opinion were extraordinarily punitive. The Court held that plaintiffs could not defend the loss adjustment with their REAs, but the Court overlooked the fact that, because the Court held that our claim for a loss adjustment could not be tried, we could not defend against plaintiffs' claim for incurred costs. For this reason, we respectfully submit that, according to the logic of December 1996 damages opinion, a decision to award plaintiffs all of their incurred costs would be as much of a "sham" as deciding the REAs, profit, and loss adjustment. Assuming plaintiffs could meet their extraordinarily heavy burden to excuse their default, then they, in effect, would be awarded a

windfall in the form of their incurred costs, only because the loss adjustment issue could not be tried.

Accordingly, for these and other reasons set forth in the following brief, we respectfully request that the Court: (1) reconsider the March 1 order in light of the procedural and substantive concerns we identify below; (2) adduce a complete factual record; (3) decide fully all issues remanded by the court of appeals; and (4) avoid an outcome that penalizes the Executive for invoking the state secrets privilege.

STATEMENT OF FACTS

A. Plaintiffs' Expansive Pre-Remand Superior Knowledge Claim

Initially, plaintiffs based their "superior knowledge" claim in Count IX upon the alleged existence of, and general failure to share information from, "classified, special access" programs involving "low observable aircraft and other weapons systems." Second Am. Unclassified Complt. ¶ 46. Plaintiffs' superior knowledge discovery was originally confined to the Air Force's B-2 and F-117A programs.

Beginning in 1993, however, plaintiffs expanded their inquiries into other highly classified matters within the Department of Defense. *See* Orders dated Mar. 5, 1993, Mar. 18, 1993, and Mar. 23, 1993. Plaintiffs' ballooning discovery requests forced Acting Air Force Secretary Michael B. Donley to invoke the state secrets privilege to protect certain other classified information. Upon mandamus review, the court of appeals upheld that invocation.

In re United States, Misc. No. 374, slip op. at 5, 9 (1993).

Following the Federal Circuit ruling, this Court stayed all superior knowledge discovery pending a determination "whether Count IX or any other claim or defense must be dismissed" due to the state secrets privilege. Order dated May 7, 1993, at 2. We filed a motion to dismiss plaintiffs' superior knowledge claims or, in the alternative, for partial summary judgment upon several grounds. For example, given its breadth at the time, we sought dismissal of plaintiffs' superior knowledge claim because, among other things, its "very subject matter" then appeared to be a state secret; plaintiffs' claim and the Government's defenses apparently were "inextricably intertwined" with facts that were themselves state secrets; and that, in any event, plaintiffs could not make out a *prima facie* case. Def. Mot. To Dismiss Pl. "Superior Knowledge" Claims, or, in the Alternative, for Partial S.J. (May 27, 1993). Plaintiffs responded that they could establish a *prima facie* case with B-2 and F-117A information, and urged that they be permitted to complete B-2 and F-117A discovery. Pl. Mot. for Continuance of Def. Mot. for Partial S.J. (Jun. 8, 1993).

Thereafter, the Court held that it could not decide the "merits" of plaintiffs' superior knowledge claim due to the Air Force's invocation of the state secrets privilege. *McDonnell Douglas Corp. v. United States*, 29 Fed. Cl. 791 (1993). Despite the Court's explicit holding that it would not decide the "merits" of their superior knowledge claim, plaintiffs

then filed a motion for summary judgment upon Count IX, relying principally upon B-2 and F-117A information. Pl. Mot. for S.J. on Count IX (Nov. 22, 1993).[1] After nearly a year of further limited superior knowledge discovery, the Court stayed all further superior knowledge discovery. Order dated Apr. 7, 1995, at 2-3.

B. The Court's December 13, 1996 Damages Opinion

In December 1995, the Court converted the default termination to one for convenience. *McDonnell Douglas Corp. v. United States*, 35 Fed. Cl. 358, 361 (1996). One year later, the Court issued its December 13, 1996 order and opinion explaining its decision not to consider loss adjustment, REAs, and profit in calculating a termination for convenience recovery. *McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 270 (1996). We appealed this ruling.

In July 1999, the court of appeals vacated the Court's December 1996 damages ruling. *McDonnell Douglas Corp. v. United States*, 182 F.3d 1319, 1329, 1333 (Fed. Cir. 1999). In its decision remanding this case to the Court the court of appeals stated:

[1] Plaintiffs' position in their 1993 motion for summary judgment directly contradicts their current position that they cannot establish their superior knowledge claim with B-2 and F-117A information. *See* Pl. Statement of Issues and Legal Stds. for Trial (Mar. 5, 2001), at 54. Plaintiffs have yet to offer any explanation for their irreconcilable positions regarding their own superior knowledge defense, as to which they bear the burden of proof.

> Because of the passage of time and of possible intervening developments, we are in no position to judge whether the risk of disclosure of state secrets will preclude adjudication, on remand, of Contractors' superior knowledge claim, and the issues of loss adjustment and reasonable profit. We think the trial court must be free to adjudicate the government's defense of its termination for default in the manner most fair and just to the parties. The trial court thus is free to reconsider this issue on remand. We express no view on the trial court's previous ruling on whether these three interrelated issues may be litigated.

Id., 182 F.3d at 1330.

C. Plaintiffs' Narrowed Post-Remand Superior Knowledge Claim

Upon remand, the Court's contention interrogatory process finally forced plaintiffs to disclose their superior knowledge claim. After years of access to the B-2 and F-117A programs, followed by plaintiffs' motion for summary judgment upon their superior knowledge claims based upon information from these programs, plaintiffs conceded in responses to contention interrogatories that their superior knowledge claim is far narrower in scope than they had alleged during earlier stages of this litigation. In contrast to the 1996 version, plaintiffs' current superior knowledge claim rests *exclusively*

upon the A-12 FSED proposal submitted by Northrop Corporation. A 359-364 (Pl. Resp. to Contention Interrog. No. 9). Thus, despite their possession of hundreds of thousands of pages of B-2 and F-117A program information, and despite their earlier motion for summary judgment based upon available B-2 and F-117A program information, *see* Pl. Mot. for S.J. on Count IX (Nov. 22, 1993), plaintiffs identify no document from either the B-2 program or the F-117A program that supports their superior knowledge claim. A 359-364 (Pl. Resp. to Contention Interrog. No. 9). Now, having been forced to divulge their claim, plaintiffs reveal that their superior knowledge claim bears no resemblance to the national security Pandora's box it appeared to be in 1996. To the contrary, plaintiffs' current superior knowledge claim implicates only unclassified and classified A-12 program information.

SUMMARY OF ARGUMENT

If interpreted to preclude admission of available evidence at trial, the March 1 order will yield an incomplete trial record, substantially increasing the likelihood that this case will be remanded back to the Court in the likely event of an appeal. If the Court does not establish an evidentiary record linking plaintiffs' superior knowledge claim to the state secrets record developed by the Court, the court of appeals will have no basis upon which to conduct a meaningful review of the Court's decision to remove the issues of superior knowledge, loss adjustment, and profit from the litigation. Thus, after an appeal, it is quite likely

that the case will be remanded for development of such a record. In light of this grim but highly certain prospect, we respectfully urge the Court to reconsider its March 1 order removing the issues of superior knowledge, loss adjustment, and profit from trial, and to adduce, at trial, a complete factual record regarding all issues and including all pertinent available evidence. Only a complete evidentiary record would permit the Court to determine finally what effect, if any, the single state secrets invocation should have upon this litigation.

In addition to our procedural concerns, we believe that the March 1 order is substantively incorrect. It is the responsibility and the prerogative of the Executive to protect national security, and it is the position of the United States that plaintiffs' current superior knowledge claim can be tried fully and safely. Although it once appeared unwieldy and amorphous, plaintiffs' actual superior knowledge claim rests exclusively upon proprietary information contained in its competitor's proposal for the A-12 FSED contract. Thus, the Court can readily decide this claim based strictly upon unclassified and classified A-12 information. There is no reason to remove the superior knowledge issue from this case based upon state secrets grounds. In any event, the legal effect of the state secrets privilege is simply to remove the covered evidence from the case. Thus, given plaintiffs' prior assurances that they could establish their superior knowledge claim based upon B-2 and F-117A information alone, the removal of privileged evidence would not preclude plaintiffs' ability to establish their superior knowledge claim.

In short, plaintiffs must proffer available evidence supporting their superior knowledge claim for admission into the record; otherwise, they will fail to meet their burden of proof.

Finally, assuming that plaintiffs could meet their extraordinarily heavy burden to excuse their manifest default, the March 1 order would raise serious concerns if the Court were to convert the termination for default to one for convenience. Contrary to established law, the March 1 order harshly penalizes the Government for invoking the state secrets privilege by removing the Government's contractual and regulatory right to apply a $1.5 billion loss adjustment, which is *five times* the amount of plaintiffs' theoretical claim for profit, and, thus, spreads the state secrets consequences in a grossly disparate fashion. An award to plaintiffs of a monetary judgment for incurred costs, without permitting the Government to prove a loss adjustment, would be as much of a "sham" as deciding the loss adjustment without permitting plaintiffs to prove their alleged superior knowledge REAs. By removing *only* loss adjustment and profit from the damages case in 1996, the court entered a $1.2 billion judgment, plus interest, that made the A-12 cancellation an affirmative benefit for plaintiffs and put them squarely at odds with their own subcontractors who suffered painful loss adjustments. Such a potential outcome from the March 1 order would be antithetical to the very nature of a termination for convenience, which is intended to place a contractor in the same position in which it would have been but for the termination.

Although we disagree with the domino-effect rationale of the December 1996 damages opinion, its logic would lead ultimately to the following conclusion: if the Court has ruled correctly that it cannot decide issues of profit and loss adjustment, then it also cannot decide, fairly, plaintiffs' termination for convenience claim. At the end of the day, the Court's own rationale would require a conclusion that -- in a termination for convenience setting -- plaintiffs could not receive an award of monetary damages. We maintain, however, that it is the prerogative of the Executive to protect national security, and all of plaintiffs' current claims and defenses are fully and safely triable.

ARGUMENT

I. The March 1 Order Raises Serious Procedural Concerns

A. An Evidentiary Record Must Be Adduced Before The Court Can Rule That Any Of Plaintiffs' Claims And Defenses Cannot Be Adjudicated

The Executive's invocation of the military and state secrets privilege serves to exclude the covered evidence from the case. *Ellsberg v. Mitchell*, 709 F.2d 51, 65 (D.C. Cir. 1983), *cert. denied*, 465 U.S. 1038 (1984). The operation of the state secrets privilege is akin to that of the attorney-client privilege, the husband-wife privilege, and the physician-patient privilege. *Id.*

As a procedural matter, the Court must develop a complete evidentiary record before it can

make a final determination as to whether it can decide the merits of plaintiffs' affirmative defenses and claims without the privileged evidence. *See United States v. Reynolds*, 345 U.S. 1, 11 (1953); *Kasza v. Browner*, 133 F.3d 1159, 1166 (9th Cir.), *cert. denied*, 525 U.S. 967 (1998); *Ellsberg*, 709 F.2d at 65 (remanding case to determine if plaintiffs can prove *prima facie* case without privileged information). In this case, the pool of potential evidence upon which the Court can decide plaintiffs' claims and defenses is massive: it includes tens of millions of pages of unclassified and classified A-12, B-2, and F-117A program information. No state secrets privilege has been asserted over any of this material.

1. Absence Of Any "Superior Knowledge" Record

The record in this case, to the best of our knowledge, does not establish a legal nexus between the claim of state secrets and plaintiffs' current superior knowledge claim. To date, *no* witness has testified either in support of or against the superior knowledge count of plaintiffs' complaint (count IX), nor has any witness provided testimony or evidence regarding the REAs that actually assert a superior knowledge theory. Indeed, plaintiffs have not introduced a single document into evidence that support their superior knowledge claim. Moreover, neither side has introduced any evidence into the record to establish that plaintiffs' superior knowledge claim cannot be tried. To date, the nexus between the Court's state secrets record and

plaintiffs' claims and affirmative defenses consists only of lawyers' characterizations of *potential* evidence.[2] Bare lawyer argument alone cannot support a legal ruling that an issue cannot be tried.

Indeed, the Court's December 1996 order relied upon vigorously disputed facts as to which no evidentiary hearing or trial has ever been held. For example, the Court relied upon deposition testimony, cited by McDonnell Douglas in a discovery pleading, that the A-12 "was to be a miniature B-2." 37 Fed. Cl. at 275 n.6 (citing Deposition of John Lehman, Jul. 26, 1995, at 104-05); *see also* Pl. McDonnell Douglas Corp.'s Mem. on Superior Knowledge Discovery in Resp. to the Court's Feb. 7, 1996 Order (Feb. 28, 1996), at 6. However, the briefs then before the Court contained the deposition testimony of Dr. David S.C. Chu of the Office of the Secretary of Defense; Admiral William Miller, Director of the Navy's Low Observable Office; and Margaret Claire Schumacher, a NAVAIR engineer, all of which flatly

[2] Indeed, the Court previously determined that the state secrets privilege relates to a potential Government defense. 37 Fed. Cl. at 280-82. As a matter of law, "if the privilege deprives the *defendant* of information that would otherwise give the defendant a valid defense to the claim, then the Court may grant summary judgment to the defendant." *Bareford v. General Dynamics Corp.*, 973 F.3d 1138, 1141 (5th Cir. 1992) (emphasis in original). Although we can defeat plaintiffs' superior knowledge claim without state secrets-related defenses, we note parenthetically that, rather than granting summary judgment in favor of the Government, the Court penalized the Government by removing its $1.5 billion loss adjustment claim from the case. *See McDonnell*, 37 Fed. Cl. at 285.

contradicts the contention that the A-12 was intended to be a "miniature B-2." *See* Def. Resp. to Pl. Status Response Concerning Superior Knowledge and the Order of Proof at Trial (Mar. 14, 1996), at 17-18 (citing Deposition of David S.C. Chu, Aug. 9, 1993, at 21; Deposition of William C. Miller, Aug. 4, 1995, at 90-91; and Deposition of Claire Schumacher, Jul. 20, 1995, at 115-16)). We respectfully urge the Court to reconsider its reliance upon disputed material fact without conducting a trial or hearing.

In short, to make any state secrets ruling procedurally sound, the Court must establish an evidentiary record to support its conclusion that information covered by the Executive's recent invocation of the state secrets privilege is, in fact, "necessary to resolution of [superior knowledge, loss adjustment, and profit] issues." March 1 order, at 2. As a procedural matter, the March 1 order is premature because it is unsupported by any evidence establishing a nexus between the Court's state secrets concerns, *see* March 1 order, at 1-3, and plaintiffs' current superior knowledge claim.

2. Absence Of Any "Impossibility" Record

Contrary to the plain language of the March 1 order, plaintiffs insist that the Court also removed their affirmative defense of impossibility upon state secrets grounds. *E.g.*, Pl. Mot. in Limine to Exclude Certain Expense Reports & Testimony (Mar. 14, 2001), at 1-2. With neither explanation nor excuse, plaintiffs suggest that they will make no attempt to meet their burden to establish their impossibility

defense until some unspecified time following the May 2001 trial. Pl. Statement of Issues and Legal Stds. for Trial (Mar. 5, 2001), at 51. Although plaintiffs allege the existence of a connection between the state secrets privilege and their ability "to complete discovery and to fully try their affirmative defenses of superior knowledge and impossibility, as well as the related defense of excusable delay," *id.* at 3, they articulate no basis for this alleged connection. More critically, the Court has entered no ruling excluding plaintiffs' affirmative defense of impossibility from the May trial.

At the March 8, 2001 hearing, counsel for General Dynamics argued that the impossibility doctrine contains only two elements: (1) "that the specifications were beyond the state of the art;" and (2) "that the government had greater knowledge or superior knowledge." Tr. (Mar. 8, 2001), at 78-79. Plaintiffs' counsel misstated the hornbook elements of an impossibility claim; in fact, as set forth in our February 12, 2001 "issues" brief, the elements of impossibility are numerous and extremely difficult for a plaintiff to establish. *See* Def. Brief Regarding Issues to be Addressed and the Appropriate Trial Stds. to be Applied at the May 1, 2001 Default Trial (Feb. 12, 2001), at 21-23 (plaintiffs bear burden to prove: (1) they did not assume the risk of impossibility; (2) no other contractor within industry could have complied with specifications; (3) they did not fail due to incompetence, mismanagement, or poor business or technical judgment; and (4) specifications required performance beyond state of

the art) (citing *J.A. Maurer, Inc. v. United States*, 202 Ct. Cl. 813, 827, 485 F.3d 588, 595 (1973); *Oak Adec, Inc. v. United States*, 24 Cl. Ct. 502, 504 (1991) (other citations omitted). Plaintiffs' failure to establish any one of the required elements would defeat their claim. The state secrets invocation does not, and would not, affect the Court's ability to decide plaintiffs' impossibility claim.

For example, plaintiffs' impossibility claim fails as a matter of law because plaintiffs concede that the technical specifications were achievable and argue instead that they could not achieve the specifications profitably. A 354-358 (Pl. Resp. To Contention Ints. 6, 7(a)). The whole of plaintiffs' impossibility defense is legally invalid. *See Natus Corp. v. United States*, 178 Ct. Cl. 1, 10-11, 371 F.3d 450, 456-57 (1967) (impossibility doctrine does not guarantee contractors can perform profitably, on-time, or within contract's ceiling price). Thus, upon this basis alone, the Court can decide fully and completely plaintiffs' impossibility claim. In any event, plaintiffs have offered no explanation whatsoever as to how or why the Court should relieve them of their burden to attempt to prove their impossibility defense at the May trial.[3]

[3] Plaintiffs argue that the parties' "relative expertise" is actually an affirmative element of impossibility that requires them, in turn, to establish each of the four elements of a legal superior knowledge claim. *E.g.*, Pl. Mot. In Limine to Exclude Certain Expert Reports and Testimony (Mar. 14, 2001), at 1-2. According to plaintiffs, because an impossibility claim by necessity incorporates each of the elements of a superior knowledge claim, the Court cannot decide their impossibility

* * *

In short, at the May 1 trial, all parties must be free to introduce any and all relevant evidence regarding plaintiffs' affirmative claims and defenses. Otherwise, the record will be devoid of any nexus linking the Court's state secrets record to those claims and affirmative defenses. Indeed, without any evidentiary record of plaintiffs' claims and affirmative defenses, the Court's state secrets ruling does not have any connection to any issue presented in this litigation.

B. Procedural Concerns Regarding The Court's *Ex Parte* Record

As in the December 13, 1996 opinion, the Court in the March 1 order refers to its "classified appendix," the contents of which have never been divulged to any party. March 1 order at 3; 37 Fed. Cl. at 285. In addition, the Court refers to "recent briefings" in the March 1 order. March 1 order at 2. We have grave concerns regarding the procedural soundness of the secret appendix and briefings. To the extent that they reflect any material not submitted by the parties, such material simply cannot form part of the record in this case, nor may

claim. *Id.* Plaintiffs' argument is preposterous. In reality, a court considers the parties' relative expertise as one of many factors in determining who warranted the design and assumed the risk of impossibility. *E.g., J.A. Maurer*, 202 Ct. Cl. at 827-28, 485 F.2d at 595-96. In this case, the evidence at trial will demonstrate that the contractors warranted their A-12 design, which General Dynamics commenced nearly a decade before the Navy had any inkling it would seek to procure a stealthy carrier aircraft.

the Court consider such material in rendering a decision in this case. Although the Court may, when necessary, conduct *in camera* review of materials properly filed, it is settled that the Court may not consider materials not submitted by the parties or that reflect judicial investigation of material outside of the record. *See, e.g., Lussier v. Runyon*, 50 F.3d 1103, 1113-15 (1st Cir.), *cert. denied*, 516 U.S. 815 (1995); *Knop v. Johnson*, 977 F.3d 996, 1010-11 (6th Cir. 1992), *cert. denied*, 507 U.S. 973 (1993); *Price Bros. Co. v. Philadelphia Gear Corp.*, 629 F.3d 444 (6th Cir. 1980), *appeal after remand*, 649 F.2d 416 (6th Cir.), *cert. denied*, 454 U.S. 1099 (1981). As such, to the extent that the Court's secret appendix or other briefings contain material not provided by either party, the Court may not rely upon such material in deciding the effect of the state secrets privilege upon this litigation.

C. Plaintiffs Enjoy Access To An Unprecedented Amount Of Information To Establish Their Superior Knowledge Claim

1. No Evidentiary Record Exists As To Effect Of The Passage Of Time Or Intervening Developments

The court of appeals asked the Court to create an evidentiary record to establish whether "the passage of time and . . . possible intervening developments" have reduced "the risk of disclosure of state secrets" to the point such that the risk "will [not] preclude adjudication, on remand, of Contractors' superior knowledge claim, and the

issues of loss adjustment and reasonable profit." *McDonnell*, 182 F.3d at 1330; *see* March 1 order at 1. Although the Secretary of the Air Force invoked the state secrets privilege over a certain matter in January 2001, *see* March 1 order at 2-3, substantial evidence exists to demonstrate that "the passage of time and . . . possible intervening developments" have ameliorated the security and state secrets concerns upon which the Court based its December 1996 ruling. *McDonnell*, 182 F.3d at 1330.

First, as discussed above, the Court's contention interrogatory process has revealed plaintiffs' superior knowledge claim to be far narrower in scope than it appeared in 1996. A 359-364 (Pl. Resp. to Contention Interrog. No. 9). This is precisely the type of "intervening development" that the Court should consider in "adjudicat[ing] the government's defense of its termination for default in the manner most fair and just to the parties." *McDonnell*, 182 F.3d at 1330.

Second, substantial evidence exists to show that security restrictions regarding B-2 and other formerly classified program data have reduced significantly since 1996. For example, the Tacit Blue was an unannounced stealth aircraft program until April 1996; today, the actual Tacit Blue is on permanent display at the United States Air Force Museum near Dayton, Ohio. A 378 (United States Air Force Museum News Release "Tacit Blue To Be Unveiled At Public Ceremony"); A 380 (United States Air Force Fact Sheet "Tacit Blue"). Numerous books about the B-2 have been published in recent years

including *Northrop Grumman B-2 Spirit: An Illustrated History*, B. Holder (A Schiffler Military History Book); *The B-2 Goes To War*, R. Grant (IRIS Press); *World Airpower Journal, "B-2 Spirit: The 'Stealth Bomber"* (Aerospace Publishing Limited); and *Inside the Stealth Bomber*, B. Sweetman (MBI Publishing Co.). Just this past February, the Air Force placed a large center-body section of the B-2 on display at the Air Force Museum. A 382 (United States Air Force Museum News Release "Stealth Bomber Slated For U.S. Air Force Museum Arrives At Wright-Patterson Air Force Base"). In addition, since 1996, the Air Force has undertaken a large-scale effort to declassify B-2 program data. Indeed, within the past few months, we completed production by releasing the relatively small balance of B-2 and F-117A documents that had been owed to plaintiffs. Thus, plaintiffs now have in their possession or access to all the B-2 and F-117A information they have requested.

In accordance with the direction of the court of appeals, the Court should establish an evidentiary record that includes this and other evidence to address the effect of the passage of time and intervening developments upon its state secrets ruling. *See McDonnell*, 182 F.3d at 1330. A complete evidentiary record is necessary for the Court to make a final determination as to whether the passage of time and intervening developments have affected its ability to decide plaintiffs' current superior knowledge claim.

2. Plaintiffs Are Free To Rely Upon All Available B-2 And F-117A Information To Establish Their Claims And Defenses At Trial

The Executive has invoked no state secrets privilege as to B-2 and F-117A program information. Indeed, plaintiffs' composites expert, Daniel B. Arnold, relies upon B-2 information in connection with default issues. Thus, although the Court suggested recently at a hearing that B-2 and F-117A program information be removed from the case, Tr. (Mar. 8, 2001), at 71-75, any exclusion of such evidence from the May trial, by necessity, would be upon grounds other than state secrets.

For years, we consistently maintained that B-2 and F-117A program evidence is not relevant, and we objected to plaintiffs' onerous production requests as a burdensome fishing expedition. We lost those arguments and were forced to produce hundreds of thousands of pages of B-2 and F-117A documents. Now, having fished for years through hundreds of thousands of pages of B-2 and F-117A documents, plaintiffs' nets evidently have come up empty.

Plaintiffs' now-admitted inability to establish a superior knowledge claim based upon the mountains of B-2 and F-117A information in their possession can and should be made part of the record of this case. B-2 and F-117A information should not be removed from the case simply because plaintiffs allege that such information would be relevant only to their removed superior knowledge claim, or

because their counsel avers that "security constraints are tougher" and "we are in worse shape today" than in 1996. Tr. (Feb. 20, 2001), at 28. Not only might B-2 and F-117A information have possible relevance to other issues in the case, plaintiffs are free to rely upon all available evidence to establish their claims and defenses at the May trial. We have a right to establish this fact in the record.

Because the Government has done nothing to preclude plaintiffs' access to B-2 and F-117A information, under no circumstances should plaintiffs be permitted to argue that Government action prevented them from making full use of all B-2 and F-117A information at the May 2001 trial. Indeed, plaintiffs can and should make full use at trial of the hundreds of thousands of pages of B-2 and F-117A information they have in their possession if they believe that this information supports their claim. In short, plaintiffs must proffer available evidence supporting their superior knowledge claim for admission into the record.

II. The March 1 Order Raises Numerous Substantive Concerns

A. Plaintiffs' Narrowed Superior Knowledge Claim Is Without Factual Or Legal Merit And Can Be Resolved Without Implicating Any State Secrets Concerns

1. The Navy Bore No Implied Duty To Divulge Classified Information

Contrary to plaintiffs' remarkable assertion that the court of appeals "supported" the existence of an underlying duty to share "superior knowledge" in this case, Pl. Statement of Issues and Legal Stds. For Trial (Mar. 5, 2001), at 53 n.27, in fact, the court of appeals expressed no view upon whether the Navy "could have an implied duty to reveal classified information pertinent to the A-12 program that would have threatened national security." *McDonnell*, 182 F.3d at 1330. In reality, the Navy bore no implied duty to share classified information with the contractors. *Department of Navy v. Egan*, 484 U.S. 518 (1988); Executive Order 12,356 sec. 4.2 (Apr. 2, 1982), 3 C.F.R. 166, 174 (1983)).[4] If the

[4] Implying a duty to reveal classified information in this case would dangerously undermine the strict security requirements governing classified information. *See Hercules, Inc. v. United States*, 516 U.S. 417, 429 (1996). Further, the Navy cannot be charged with the "superior knowledge" of the Air Force. *See, e.g., Bethlehem Corp. v. United States*, 199 Ct. Cl. 247, 254, 462 F.2d 1400, 1404 (1972) ("The fact that there were humidity experts in the National Bureau of Standards with superior

contractors expected to receive data from other compartmented, classified programs, then they should have negotiated a provision for such data in the contract's Government-furnished information ("GFI") clause. Because the sophisticated contractors in this case negotiated the contract's GFI clause without any such provision, the existence of a provision to provide classified information may not be inferred.

c. In Any Event, The Available Evidence Demonstrates That Plaintiffs' Superior Knowledge Claim Is Both Without Merit And Capable Of Fair, Safe, And Complete Adjudication

To avoid a failure of proof regarding their superior knowledge claim, plaintiffs bear the burden to proffer specific evidence that: (1) they undertook to

knowledge who would have anticipated the technical difficulties here encountered is immaterial."); *Fansteel Metallurgical Corp. v. United States*, 145 Ct. Cl. 496, 172 F. Supp. 268, 271 (1959) (one branch of the government cannot be attributed with knowledge reposed in files of other department units). Finally, contractors working on other classified programs always had possession of any alleged "superior knowledge"; accordingly, any alleged superior knowledge was never within the Navy's exclusive possession. *See Giesler v. United States*, 232 F.3d 864, 877 (Fed. Cir. 2000) (contractor in privity with subcontractor had "equal, if not greater access" to alleged superior knowledge); *H.N. Bailey & Assocs. v. United States*, 196 Ct. Cl. 166, 178, 449 F.2d 376, 382-83 (1971) ("The government is under no duty to volunteer information in its files if the contractor can reasonably be expected to seek and obtain the facts elsewhere.").

perform the contract without "vital" knowledge of a fact affecting performance, costs, or duration; (2) the Navy knew the contractors had no knowledge of, and had no reason to obtain, the "vital" information; (3) any contract specification supplied misled them, or did not put them on notice to inquire; and (4) the Navy failed to provide the relevant information. *See Giesler v. United States*, 232 F.3d 864, 876 (Fed. Cir. 2000); *American Ship Bldg. Co. v. United States*, 228 Ct. Cl. 220, 225, 654 F.2d 75, 79 (1981). Plaintiffs must establish that the information not shared was *vital* to their successful performance of the contract, not simply relevant. *Granite Constr. Co. v. United States*, 24 Cl. Ct. 735, 744 (1991). Available evidence never heard by the Court demonstrates plaintiffs' inability to meet their burden, regardless of state secrets information.

Following remand, plaintiffs reduced dramatically the scope of their superior knowledge claim to concern only the Navy's alleged failure to share superior knowledge from other classified programs regarding weight, schedule, and cost that were essential to bidding on and to performing the A-12 contract. Pl. Mem. In Opp. to the Govt.'s Mot. To Compel Disclosure (Jan. 31, 2001), at 14-16; Pl. Resp. To "Def. Statement Of Issues And Notice Of Probable Testifying Experts For Trial" (Jul. 25, 2000), at 14-15. Thus, after ten years of litigation, plaintiffs finally abandoned their complaint's general, non-specific claim of superior knowledge,

and radically circumscribed their superior knowledge claim to three areas: weight, schedule, and cost.[5]

Moreover, plaintiffs rely upon none of the hundreds of thousands of pages of F-117A and B-2 documents we produced to them over several years to support their current superior knowledge claim. They concede that the supposedly "vital" weight, schedule, and cost information is contained exclusively within Northrop's A-12 proposal. A 359-364 (Pl. to Resp. Def. Cont. Interrog. No. 9). However, as plaintiffs are well aware, statute and regulation *prohibited* the Navy from disclosing Northrop's proposal or proprietary information to the contractors during source selection.[6]

a. The Navy Provided Any Required Warning

To the extent that the Navy might have borne a duty to provide a "general warning" pursuant to *J.A. Jones Constr. Co. v. United States*, 182 Ct. Cl. 615, 390 F.2d 886 (1968), the available evidence demonstrates conclusively that the Navy provided

[5] Although plaintiffs never identified the specific problems and solutions allegedly withheld from them, they generally framed their superior knowledge claim as encompassing highly technical aspects of stealth technology design and integration.

[6] Pursuant to the Procurement Integrity Act, no person may disclose proprietary or source selection information "to any person other than a person Authorized by the head of such agency or the contracting officer to receive such information." 41 U.S.C. § 423(d). The Federal Acquisition Regulation ("FAR") prohibits technical leveling or technical transfusion by sharing technical information contained in a competitor's proposal. 48 C.F.R. § 15.601.

such a warning. The Navy warned the contractors during contract negotiations that their proposed weight guaranty should have been at least 2,000 pounds higher. A 106 (Jun. 1, 1987 Discussion Information Request). The Navy provided its detailed analysis of the contractors' weight estimate to the contractors, and identified specific areas in which the contractors had underestimated the weight of their design. In defiance of the Navy's warning, the contractors incorporated only a modest portion of the Navy's recommended weight increase. Plaintiffs' only response in litigation to this undeniable fact is that:

> During the B-2 briefings which we received, . . . we were told that the B-2 had significant weight growth problems during development *[but] we were not given, nor have we ever received details* . . . . Had [we] known and understood the *details* . . . of B-2 weight growth, our approach to the A-12 design development would have been substantially modified.

A 365-366 (Farr Decl. at ¶¶ 57-58 (emphasis added)). Thus, plaintiffs, at bottom, do not complain of a failure to provide a general warning; rather, in direct contravention of Supreme Court precedent, they base their superior knowledge claim upon an implied duty to divulge information that was compartmented and highly classified in 1988. *See Department of Navy v. Egan*, 484 U.S. at 527.

b. Nothing In Northrop's A-12 Proposal Was "Vital"

Regardless of state secrets, plaintiffs' superior knowledge claim also fails because they cannot establish that information in Northrop's proposal was vital to the contractors' performance of the A-12 contract. Putting aside the impropriety that would have occurred had the Navy revealed Northrop's competitive-sensitive information to the contractors, plaintiffs still refuse to provide specific details as to how proprietary information unique to Northrop and Northrop's own A-12 proposal would have caused the contractors to change their approach to their own proposal. Available evidence refutes plaintiffs' unfounded speculation that Northrop's proposal documents somehow contained information "essential" to the contractors' ability to estimate accurately the weight, schedule, and cost of the contractors' own design.

1. *Weight.* As established above, the Navy, in fact, issued a "general warning" to the contractors that their aircraft weight estimate was at least 2,000 pounds too low. Because the contractors largely ignored the Navy's recommended increase in the guaranteed weight, Plaintiffs now contend that they would have heeded the Navy's "general warning" if only the Navy had improperly, if not illegally, disclosed Northrop's proposal to them and revealed that Northrop had calculated a 9.4 percent weight penalty for its unique A-12 design. A 359-364 (Pl. Res. Def. Cont. Interrog. 9(A)).

For the sake of argument, if the contractors had applied a 9.4 percent weight penalty used by Northrop to the contractors' own proposed vehicle, the contractors' weight estimate would have been approximately 3,500 pounds higher. Available evidence demonstrates that the 9.4 percent weight penalty is entirely immaterial because, prior to award, the contractors knew or should have known, for reasons entirely unrelated to Northrop's weight estimation methodology, that the contractors' weight estimate should have been at least 3,500 to 4,000 pounds higher than their proposed weight guaranty.

Prior to award, the contractors knew that a "bottoms up" or "rough order of magnitude" ("ROM") estimate of the aircraft structural weight would have yielded the most accurate weight estimate available at that stage in the program. Indeed, the contractors contemplated performing such a weight estimate prior to award. However, the contractors postponed the ROM estimate for purely business reasons. A 385-386 (Lamers Dep. Vol. 8 (Mar. 1, 2001), at 291-293). Approximately four months after award, the contractors finally conducted a ROM weight estimate and confirmed that they had underestimated the structural weight of their design by between 3,500 and 4,000 pounds. A 213 (Jun. 13, 1998 Weight Growth Concern Mem.); A 218 (Jul. 5, 1988 Minutes of Weight Control Board). The contractors required no "superior knowledge" from Northrop to perform this ROM estimate.

Prior to award, the contractors were well aware of the benefits of performing a ROM estimate

and simply chose to forgo those benefits.[7] Given the Navy's "general warning" and the contractors' business decision to postpone obtaining a more accurate weight estimate until after award, plaintiffs cannot establish any causation between the Navy's alleged "superior knowledge" by virtue of its simple receipt of the Northrop proposal, and the contractors' multiple failures to address the known inadequacy of their weight estimate. The superior knowledge doctrine does not relieve a contractor from the consequences of its ill-advised business judgment. *American Ship Bldg.*, 228 Ct. Cl. at 225, 654 F.2d at 79 (it is "reasonable for the government to assume that a contractor is the best judge of its competency and will exercise good judgment in deciding to bid on a contract.").

2. *Proprietary Cost Information.* Plaintiffs also complain that the Navy did not share Northrop's cost information with them. In essence, plaintiffs argue that they would have proposed a higher price had the Navy improperly, if not illegally, disclosed Northrop's proprietary cost information to them. A 360 (Pl. Resp. to Contention Interrog. No. 9). Not only do plaintiffs base their superior knowledge claim upon the Navy's failure to violate rules and regulations, they really, at bottom, complain of a

[7] The contractors' business decision was especially risky given the substantial risk they recognized for their structural weight estimate. A 179 (Sept. 2, 1987 Weight Review recognizing high risk weight items including the "basic airfoil structure"); A 37 (Feb. 1987 Mem. Re: Model 21 Weight Control Plan again recognizing the need for a strong weight control program because of such high risk items as the "basic airfoil structure").

mistake in bid claim. Plaintiffs essentially argue that the price disparities between their proposal and that of Northrop required the Navy to verify that their proposal contained no mistake. *See, e.g., McClure Elec. Constructors, Inc. v. Dalton*, 132 F.3d 709, 710 (Fed. Cir. 1997). However, plaintiffs could obtain relief only if they established that their "bid error resulted from a 'clear cut clerical or arithmetical error, or a misreading of the specifications.'" *Giesler*, 232 F.3d at 869 (quoting *Liebherr Crane Corp. v. United States*, 810 F.2d 1153, 1157 (Fed. Cir. 1987)). As this Court stated in *Dakota Tribal Indus. v. United States*, 34 Fed. Cl. 593 (1995), a contractor may not obtain relief for a mistake in bid that resulted from an error in judgment, that is:

> where the bidder has the facts necessary to make the proper conclusion but, because of improper assumptions or faulty assessments of those facts, makes a bad business decision. Such a "conscious gamble with known risks" is non-compensable.

Id. at 596 (citations omitted).

At best, plaintiffs' arguments regarding Northrop's A-12 proposal corroborate the contractors' exercise of poor business judgment. For strictly competitive reasons, the contractors deliberately increased their risk under a fixed price contract by deciding to take a "management challenge" to reduce their proposed fixed price by slicing 7.5 percent from their internal cost estimates. A 172A-172E (BAFO

Price Report). In any event, plaintiffs cannot establish any harm from the nondisclosure of Northrop cost information because the difference between the two teams' cost proposals is insignificant when costs are normalized for, among other things, differing overhead and labor rates. A 291. Indeed, the Navy perceived no vital information in the Northrop proposal that would have assisted the contractors in estimating cost or schedule. Dorsett Dep. (Aug. 22, 1995), at 103 ("What I'm really saying here is Northrop did nothing in the estimating to lead you to believe that they thought the plane was going to be harder to build or more expensive than McDonnell Douglas/GD. In fact, just the opposite was true.").

3. *Schedule.* The contractors proposed a 30 month to first flight schedule because their management decided to propose an aggressive schedule to win the contract. Internally, others, including Dr. Jackson, had advocated proposing a longer schedule. A 307 (Jackson Dep. (Jun. 20, 1995), at 9-10). Moreover, to the extent plaintiffs now claim they would have proposed a first flight schedule between 40 and 50 months, the Navy's unilateral schedule extension in August 1990 cured any alleged harm by increasing the first flight schedule to 48 months. A 339 (Lamers Dep. (Sept. 14, 1995), 60-61).

At bottom, the contractors made a calculated business decision to submit an aggressive proposal for the A-12 contract. At all times, they were well aware of the risks they were taking, with or without

access to Northrop information. Because the Navy is not the guarantor for the contractors' ill-fated business decisions, available evidence can defeat plaintiffs' superior knowledge claim, regardless of state secrets. *See Dakota Tribal Indus.*, 34 Fed. Cl. at 596.

c. The Contractors Resisted Access To B-2 and F-117A Information

Both before and after contract award, the contractors enjoyed numerous opportunities to obtain any information they believed was relevant (or vital) to their performance of the A-12 contract.

1. *Knowledge of B-2 Prior to Award.* The contractors knew of the existence of the unacknowledged B-2 program long before they submitted their A-12 proposal. For example, nearly two years before contract award, John Lamers, General Dynamics' program manager, recognized that Northrop held a "technical advantage in stealth because of ATB [B-2] and other experience." A 2 (Apr. 10, 1986 briefing slide "Review of Competitive Situation"). Similarly, Keith Jackson, General Dynamics' chief engineer, concedes that he was aware at least two years before the A-12 contract was awarded that the B-2 program involved the development of a stealth bomber. A 351-352 (Jackson Dep. (Feb. 22, 2001), at 491-92). Thus, prior to award, the contractors were aware of the B-2 program and any arguable relevance to the A-12 program.

Available evidence establishes that the contractors sought and obtained access to relevant

information from other classified programs prior to contract award. For example, two years before award, the contractors submitted to the Navy a lengthy, specific request for various information contained in other classified programs. A 3 (May 22, 1986 Technical Request). Dr. Jackson summarized the response received as follows:

> We have received some feedback on our request for technology transfer from other classified programs. It is mostly in the form of a list of people working various topics. We can contact the companies/people directly (assuming we're not already working with them). If we have any problems with clearances the customer has offered to help if they can.
>
> * * *
>
> It is possible that some more information may come out later, but the timing is uncertain. We probably can't count on much before our proposal.

A 33 (Jul. 10, 1986 Mem. Re: Technology Transfer/Technical Request). Although the contractors were aware that the B-2 program involved a stealth aircraft, they did not request relevant information about that program as part of this technical transfer.[8]

[8] Further, none of the B-2 information requests submitted by the contractors in 1988 specifically addressed the areas of B-2 weight, schedule, or cost. A 251 (Aug. 30, 1988 memorandum

2. *Subcontract with Lockheed and Access to F-117A Technology.* Plaintiffs have abandoned their superior knowledge claim based upon F-117A program information, perhaps because the contractors enjoyed access to the experience and expertise of the F-117A 's prime contractor, Lockheed, before they were awarded the A-12 contract.[9] Indeed, prior to award, General Dynamics described Lockheed's A-12 work as "critical to the success of a very low observable (VLO) aircraft program." A 35 (Nov. 25, 1986 Sole Source Justification Mem.). In their BAFO, the contractors represented to the Navy: "MCAIR and GDFW are industry leaders in developing and applying signature reduction technologies to operational tactical aircraft." A 79 (Mar. 6, 1987 proposal Executive Summary). They added that "to assure the best VLO technology experience available, particularly in the area of RCS, the MCAIR/GDFW team has utilized Lockheed and Rockwell International as subcontractors during the DEM/Val phase." *Id.* Given the contractors' claimed experience, their subcontract with Lockheed, and their pre-award access to other classified programs, the contractors were not denied access to F-117A or other stealth technology information prior to contract

concerning information on the B-2 aircraft to be provided to the A-12 program).

[9] Although A-12 engineers were not read into the F-117A program until 1989, Lockheed had provided General Dynamics with access to all of the technology developed for the F-117A the year before contract award. A 329 (Ware Dep. (Aug. 22, 1995), at 69-70).

award, nor were they unable to foresee the potential relevance of that technology to their A-12 work.[10]

3. *Contractors' Post-Award Resistance To B-2 Technology Transfer.* After contract award, the contractors could have worked directly with the Northrop engineers who built the B-2 and applied their knowledge and experience to the A-12 program, However, for purely business reasons, the contractors consciously forfeited this opportunity. To the extent that plaintiffs complain they lacked access to B-2 technologies and experience,[11] they have no one to blame but themselves. Immediately after contract award, the Navy actively encouraged the contractors to engage directly with Northrop to learn about its B-2 work. A 369-370 (Cook Decl. (Dec. 21, 1993), at ¶ 4; A 298 (Cook Tr. Vol. IV (Jul. 9, 1993), at 126; A 325 (Parr Dep. (Aug. 1, 1995). at 133.) Pike Farr, McDonnell Douglas' chief engineer, refused to participate in a direct technology interchange with Northrop "because of the possibility of proprietary

[10] The contractors' BAFO never made contract performance contingent upon access to other classified program information. In fact, the contractors assured the Navy that they, together with their subcontractors, Lockheed, Rockwell International and Brunswick, possessed "unequaled real-world experience" with stealth technology and that "the broad range of flight-proven materials and components available" to them would ensure success. A 175. Similarly, the A-12 contract did not make the contractors' performance contingent upon access to information from other classified programs.

[11] A limited number of A-12 engineers were read into the B-2 program in 1988. However, the contractors did not cease their resistance to a direct exchange of B-2 classified information with Northrop until 1990.

rights infringement, that is Northrop proprietary rights infringement." A 322 (Farr Dep. (Aug. 1, 1995), at 114). After agreeing to a direct exchange with Northrop, A 243 (August 15, 1988 Proprietary Data Rights Agreement), General Dynamics acceded to McDonnell Douglas' resistance; however, Dr. Jackson continued to feel that a face-to-face dialogue with Northrop would have been a more effective way of sharing information. A 313 (Jackson Dep. (Jun. 21, 1995), at 89-90).[12] Although the Air Force granted Mr. Farr and Dr. Jackson access to B-2 classified information in September 1988, it briefed them about the program, in accordance with Mr. Farr's demands, in the absence of any Northrop personnel. A 324 (Farr Dep. (Aug. 1, 1995), at 125).

Two years after contract award, the Navy succeeded finally in convincing the contractors to abandon their resistance to a free and open exchange with Northrop. A 371 (Cook Decl. (Dec. 21, 1993), ¶ 11; A 256 (MOU For Technical Transfer Between B-2 and A-12 Programs). Once briefed by Northrop

[12] The contractors likewise declined direct access to F-117A technology. The contractors' access to those technologies during earlier phases of the A-12 program caused them to conclude that they were obsolete by the time of contract award. Citing Lockheed's marginal technical benefit, General Dynamics severed its relationship with Lockheed shortly after contract award. A 255 (May 12, 1988 memo from John Lamers concerning the Lockheed termination); A 302 (Lamers Dep. (Jan. 5, 1994), at 233-34 (meaning of "marginal technical benefit"); A 329 (Ware Dep. (Aug. 22, 1995), at 71 (manager of Lockheed DEM/Val subcontract agreed Lockheed offered General Dynamics all technology contained in F-117A program)).

engineers regarding B-2 technical information, the contractors concluded that B-2 technical data was never vital to their performance of the A-12 contract. For example, Dr. Jackson admitted that the contractors' performance of the A-12 contract would have been unaffected by earlier access to the B-2 program because the B-2 used "fairly old technology." A 261 (Notes of K. Jackson Interview); A 317 (Jackson Tr. Jun. 21, 1995 at 173-74). Similarly, Robert Magnus, General Dynamics' lead signature engineer, conceded that earlier access to B-2 technology would not have affected the contractors' A-12 design or the price they proposed. A 272 (Notes of R. Magnus Interview); A 342-343 (Magnus Tr. Sept. 15, 1995 vol. II. at 77-79).

In short, the Navy never had any reason to believe that the contractors lacked information, and it never possessed any duty to disclose information that was equally available to the contractors. *See J.F. Shea Co. v. United States*, 4 Cl. Ct 46, 53 (1983); *see also Petrochem Servs. Inc. v. United States*, 887 F.2d 1076, 1079 (Fed. Cir. 1988); *McCormick Constr. Co. v. United States*, 18 Cl. Ct. 259, 265 (1989), *affd*, 907 F.2d 159 (Fed. Cir. 1990); *Granite*, 24 Cl. Ct. at 744. The contractors' lead engineers and managers believed that A-12 technology surpassed B-2 and F-117A technology and that nothing in those programs would have caused them to do anything differently in bidding on the A-12 contract. Regardless of the state secrets invocation, plaintiffs cannot possibly establish that the Navy failed to disclose or warn them about "vital" information derived from the B-2 and F-117A programs. In

short, plaintiffs' current superior knowledge claim is completely triable.

B. The Legal Effect Of The State Secrets Privilege Is Simply To Remove Covered Evidence From The Case, Or, In The Rare Case, To Require Dismissal Of Plaintiffs' Claim

A complete evidentiary record would permit the Court to determine conclusively the effect of the Air Force's invocation of the state secrets privilege. Generally, the Executive's invocation of the military and state secrets privilege serves to exclude the covered evidence from the case. *Ellsberg*, 709 F.2d at 65. In this case, a complete evidentiary record would establish that removal of the covered evidence does not affect the Court's ability to decide completely all of plaintiffs' claims and defenses. Such a record would demonstrate further that the Court could decide plaintiffs' REAs if the Court were to convert the default termination to one for convenience.

If, however, a complete evidentiary record were to establish that this is the rare case in which the Court could not decide safely certain of plaintiffs' claims or affirmative defenses, then the Court would simply remove the claim or defense itself, regardless of whether plaintiffs could state a *prima facie* case. *See, e.g., Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1144 (5th Cir. 1992) (merits of controversy "inextricably intertwined" with privileged matters); *Farnsworth Cannon Inc. v. Grimes*, 635 F.2d 268, 281 (4th Cir. 1980) (*en banc*). Matters that can be safely tried without jeopardizing national security

should not be removed. *See Reynolds*, 345 U.S. at 11; *Kasza*, 133 F.3d at 1166; *Ellsberg*, 709 F.2d at 65 (remanding case to determine if plaintiffs can prove *prima facie* case without privileged information). Further, dismissal of any of plaintiffs' claims or defenses would be contemplated only as a last resort. *See id.*

Plaintiffs contend that the Court's inability to decide any one of their claims means that we cannot meet our burden to sustain the default. Thus, they currently do not contest the Court's March 1 order removing their superior knowledge claim because they are hopeful that it will lead to another $1.2 billion judgment in their favor. If, however, the Court were to reject plaintiffs' apparent argument that the invocation of the state secrets privilege excuses entirely their manifest default, then there can be no doubt that plaintiffs will challenge belatedly the Court's March 1 order removing their superior knowledge affirmative defense and claim from this case.

Plaintiffs cannot cite any legal precedent for undoing the Navy's valid termination for default. Plaintiffs chose to bring suit in this Court to challenge the Navy's valid administrative process. They bear the burden of proof regarding their affirmative claims and defenses. *See CJP Contractors, Inc. v. United States*, 45 Fed. Cl. 343, 371 (1999); *Florida Eng'd. Const. Products Corp. v. United States*, 41 Fed. Cl. 534, 538-99 (1998); *Hannon Elec. Co. v. United States*, 31 Fed. Cl. 135, 143 (1994). That certain of their claims cannot be

tried in this Court simply means that they encounter a failure of proof in attempting to challenge our default claim. *See* Tr. (Mar. 8, 2001), at 79 ("MS. LISTROM: . . . we're going to have a failure of proof on our affirmative defense."). A failure of proof by plaintiffs would require the default to stand. To permit the invocation of the state secrets privilege to undo the Navy's valid administrative process -- and then to exempt plaintiffs' termination for convenience recovery from a $1.5 billion loss adjustment -- would make plaintiffs' recovery more "'unconscionable'" than Admiral Morris ever imagined. *McDonnell*, 182 F.3d at 1328 (quoting Morris testimony (J.A. 3920)). Even if the Court were permitted to fashion a unique outcome flowing from the invocation of the state secrets privilege, the outcome proposed by plaintiffs -- awarding them a $1.2 billion plus interest benefit from the A-12 cancellation -- would be grossly inequitable.

C. The March 1 Order Potentially Could Grant Plaintiffs' REAs Without A Trial Or Admitting Evidence In Their Support

For the reasons discussed in our February 12, 2001 "issues" brief, plaintiffs' default in this case is, or should be, beyond dispute. Furthermore, plaintiffs will be unable to sustain their extraordinarily heavy burden to prove that their manifest default was excused. Notwithstanding, if the Court were to convert the default termination for one for convenience, the March 1 order would render the record after trial fatally incomplete.

There is no question that plaintiffs were in a loss position at termination. *McDonnell*, 182 F.3d at 1322, 1323, 1332; *see also McDonnell Douglas Corp. v. United States*, 35 Fed. Cl. 358, 362 (1996). By removing the loss adjustment and awarding plaintiffs' nearly all of their unadjusted costs, the Court's December 13, 1996 order granted, in effect, all of plaintiffs' REAs in full, without a shred of evidence in the record to support *any* of those claims. If re-adopted, such an outcome would be expressly prohibited by *Servidone Constr. Corp. v. United States*, 931 F.2d 860, 860 (Fed. Cir. 1991) (record must contain evidence supporting any equitable adjustment in the contract's ceiling price). Moreover, some of plaintiffs' REAs have nothing whatsoever to do with superior knowledge. Thus, the March 1 order potentially could award plaintiffs full recovery for REAs that are, under any circumstances, no less triable than the basic issues of default and waiver to be tried in May, but for which plaintiffs will have proffered no evidence to carry their burden to prove the liability, causation, and pricing elements of those REAs.

Accordingly, the March 1 order creates the possibility of removing the mandatory loss adjustment without *any* evidence in the record to support even a remote possibility that plaintiffs' REAs could be sufficient to offset the vital effect of the contract's loss adjustment clause, which must be enforced. *See Madigan v. Hobin Lumber Co.*, 986 F.2d 1401, 1403 (Fed. Cir. 1993) ("A long line of our precedent has established that agreed-upon contract terms must be enforced."). In fact, with all due

respect, the record contains no support for the Court's December 1996 statement that the Government "likely could not establish application of a loss ratio" if "plaintiffs were permitted to prove their superior knowledge claim." 37 Fed. Cl. at 274. To the contrary, based upon facts found to date, *e.g.*, *McDonnell*, 182 F.3d at 1322, 1323, 1332; *McDonnell*, 35 Fed. Cl. at 362, the Government's FSED estimate at completion ("EAC") of at least $8.2 billion, and our Lot I EAC of $1.6 billion, plaintiffs' REAs, even assuming plaintiffs could meet their heavy burden to establish liability, causation, and pricing, would not offset substantially the effect of the mandatory loss adjustment.

III. The March 1 Order Could Lead To Another Error

A. The Court May Not Penalize The Government For Invoking The State Secrets Privilege

In its December 1996 damages opinion, the Court expressly sought to "sprea[d] the consequences of a difficult and dangerous problem." *McDonnell*, 37 Fed. Cl. at 285. Because the December 1996 order and opinion removed our $1.5 billion loss adjustment claim, which was five times the amount of plaintiffs' removed claim for theoretical profit, we respectfully submit that the Court "sprea[d] the consequences" of the Executive's invocation of the state secrets privilege in a sharply uneven manner that severely penalized the Government for invoking the state secrets privilege.

The effect of the Court's December 1996 order was, and potential effect of the March 1 order remains, extraordinarily punitive to the Government. In its December 1996 order, the Court relied upon the invocation of the state secrets privilege -- as to a matter concerning at most a Government defense -- to avoid reducing plaintiffs' termination for convenience claim by *over $1.5 billion* as required by the contract and the Federal Acquisition Regulation. *See* 37 Fed. Cl. at 280-82. Thus, even if the Court "clipped . . . $100 million of [plaintiffs'] costs" in excess of the undisputed funding cap, Tr. (Mar. 8, 2001), at 85, the December 1996 order would have "clipped" over $1.5 billion from the United States Treasury. In contrast, plaintiffs' removed claim for profit amounted to only $300 million, and even that amount was purely theoretical because the undisputed funding cap barred every penny of plaintiffs' profit claim. Thus, rather than "sprea[ding] the consequences" in an equitable fashion, 37 Fed. Cl. at 285, the Government alone suffered all of the consequences of the state secrets invocation. Such a result would contradict directly the settled rule that the Government cannot be "punished for asserting the privilege." *Salisbury v. United States*, 690 F.2d 966, 975 (D.C. Cir. 1992). *See In re United States*, 872 F.2d 472, 476 (D.C. Cir.), *cert dismissed*, 493 U.S. 960 (1989) ("Notions of sovereign immunity preclude any further adverse consequence to the government, such as alteration of procedural or substantive rules.").

Further evidence of the punitive nature of the December 1996 damages opinion is its inconsistency

with the contractors' virtually uniform enforcement of the loss adjustment provisions in their prime/subcontractor contracts, which mirrored the A-12 contract's provisions, to reduce substantially their subcontractors' termination for convenience recoveries. *See, e.g.*, A 346 (Yochum Dep. (Jun. 26, 1996), at 31-32; A 375-377 (Wright Trial at 230-32); A 348 (Broesche Dep. (Jul. 30, 1996), at 105-106. Thus, the December 1996 damages opinion had the effect of: (i) forcing the Government, which spent billions for no airplane, to bear the consequences of the failure of the A-12 program; (ii) countenancing the A-12 subcontractors' losses of hundreds of millions of dollars due to loss adjustments; and (iii) making plaintiffs almost completely whole. In short, the December 1996 damages opinion allocated *all losses* to the Government and the A-12 subcontractors, and relieved plaintiffs of all financial responsibility for their aggressive business judgments and failed contract performance.[13]

[13] The contractors applied an average loss adjustment adjustment of 66 percent to their subcontractors. No monetary judgment in a termination for convenience setting would lead to the same outcome. Theoretically, if plaintiffs were to be treated as their subcontractors, they would be entitled to no affirmative recovery, having already received $2.67 billion in progress payments.

B. The Rationale Of The December 1996 Damages Ruling Would Preclude A Decision On the Amount Of Plaintiffs Termination For Convenience Claim

Even if the Court's analysis of *Molerio v. Federal Bureau of Investig.*, 749 F.2d 815 (D.C. Cir. 1984), were correct, the Court's own interpretation of *Molerio*, as applied in the Court's December 13, 1996 opinion, would lead to a ruling that plaintiffs' entire claim for damages cannot be decided, not a ruling that only the mandatory loss adjustment of over $1.5 billion and plaintiffs' comparatively minor claim for profit cannot be decided.

In that December 1996 opinion, the Court reasoned that it was "unfair" to apply the loss adjustment if the state secrets privilege deprived plaintiffs of an attempt to reduce the effect of the loss adjustment by proof of their superior knowledge REAs. 37 Fed. Cl. at 274, 280-81, 285. By removing only loss adjustment and profit from the damages case in 1996, the Court decided the amount of plaintiffs' termination for convenience claim; however, that amount was no less a "sham" because we were prohibited from presenting evidence to reduce it by our defense of the $1.5 billion loss adjustment. *See id.* at 285. Under the Court's own reasoning, the decision to award plaintiffs the full amount of their unadjusted termination for convenience claim was just as much of a "sham" as the Court's rulings regarding loss adjustment and profit would have been. *Id.* It was, therefore, grossly unfair to award plaintiffs their total costs when the

Government was deprived of a defense which would have adjusted the amount of those costs as required by the contract and the Federal Acquisition Regulation.

Although the Court is not free to fashion an unique outcome flowing from the invocation of the state secrets privilege, the ultimate outcome of the domino-effect rationale of the Court's December 1996 damages opinion -- that is, even in a termination for convenience setting -- plaintiffs could not be awarded a judgment for the amount of their incurred costs. No attempt to "sprea[d] the consequences" of a state secrets invocation should countenance granting plaintiffs a reward of $1.5 billion that would place them in a far better position than if then-Secretary Cheney had granted their request for a financial bailout, pursuant to which the contractors proposed to "absorb a $1.5 billion fixed loss on the cost overrun from the contract . . . [and] waive their claims for equitable adjustment." *McDonnell*, 182 F.3d at 1323. Rather, if the rationale of the December 1996 damages opinion were correct, its logic leads to a conclusion that the Court cannot decide the amount of plaintiffs' termination for convenience claim. In the end, however, the merits of plaintiffs' excuses are insufficient to sustain their burden to excuse their manifest default.

CONCLUSION

We respectfully request that the Court develop a complete evidentiary record at the May trial so as to preclude the possibility of another remand directing development of a record to address the

Court's removal of superior knowledge, loss adjustment, and profit from the litigation. In addition to our procedural concerns, we respectfully request that the Court reconsider the substantive merits of its March 1 order. First, plaintiffs' now-compressed superior knowledge claim can be readily decided based strictly upon unclassified and classified A-12 information; thus, there is no longer even a theoretical ground upon which to remove plaintiffs' current superior knowledge affirmative defense from this case based upon state secrets grounds. Second, as a matter of law, the effect of the state secrets privilege is simply to remove the covered evidence from the case. We respectfully urge the Court to attempt to decide all remanded issues in the absence of the covered state secrets evidence. Third, we respectfully submit that the rationale of the Court's December 1996 termination for convenience damages opinion, as re-adopted in the March 1 order, assesses an unjustifiable and exorbitant penalty against the Government. The Court's December 1996 opinion deprived the Government of its contractual right to apply a $1.5 billion loss adjustment. Indeed, although we disagree with the rationale of the Court's December 1996 damages opinion, its logic outcome would be for the Court to conclude that deciding the amount of plaintiffs' termination for convenience claim, too, would have been a "sham," thereby leaving plaintiffs with no claim. The logical outcome was not entry of a $1.2 billion judgment plus interest, benefitting plaintiffs far more than even a financial bailout by then-Secretary Cheney. Accordingly, we respectfully

request that the Court: (1) reconsider the March 1 order; (2) develop a complete factual record at the May trial; (3) decide all remanded issues upon the merits, whereby issues would be removed upon state secrets grounds only as a last reason; and (4) avoid an outcome that penalizes the Government for invoking the state secrets privilege.

Respectfully submitted,

STUART E. SCHIFFER
Deputy Assistant
Attorney General

/s/ DAVID M. COHEN
DAVID M. COHEN
Director

/s/ BRYANT G. SNEE
BRYANT G. SNEE
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OF COUNSEL:

GEORGE P. WILLIAMS
Office of General Counsel
Department of the Navy

Dated: March 28, 2001

Attorneys for Defendant

No. 91-1204C
(JUDGE HODGES)

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION
AND GENERAL DYNAMICS CORPORATION,

Plaintiffs,

V.

THE UNITED STATES,

Defendant.

APPENDIX TO DEFENDANT'S BRIEF REGARDING EFFECT OF STATE SECRETS AND MOTION FOR RECONSIDERATION
VOL I of IV

STUART E. SCHIFFER,
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Washington, D.C. 20530
Tele: (202) 514-7300

Dated: March 28, 2001

Attorneys for Defendant

[REDACTED]

Review of Competitive Situation (u)

- E/W TEAM HAS TWO MAJOR, NON-TECHNICAL ADVANTAGES
  - ✓ Grumman Business Base as Navy Contractor
  - ✓ California, New York, Texas Political Base
- . . . AND NORTHROP HAS A TECHNICAL ADVANTAGE IN STEALTH BECAUSE OF ATB AND OTHER EXPERIENCE
- N/S TEAM HAS SEVERAL STRENGTHS
  - ✓ Deeper Overall Technical Capability
  - ✓ Recent Systems Integration Experience on Advanced Fighters
  - ✓ A Better "Balanced" Design Concept
  - ✓ Better Navy Interface
- KEY ISSUE: STEALTH COMPETITIVENESS

[REDACTED]

10 July 1986

Memo to: Distribution

From: S. K. Jackson, Jr.

Subject: Technology Transfer

Reference: Technical Request, 208//01X823-86

We have received some feedback on our request for technology transfer from other classified programs. It is mostly in the form of a list of people working various topics. We can contact the companies/people directly (assuming we're not already working with them). If we have any problems with clearances the customer has offered to help if they can.

The following is a list of requested topics and data sources:

- Electrically Switched Materials: Radant.
- Windshields & Transparencies: McAir (Outlaw Phantom), OTI/Brunswick.
- GASM: Dave Stegman is a contact as is John Clinton. They are working some kind of associate contractor arrangement for us.
- Engine Noise: Charlie Jackson at NASA Langley. Glen Varney of G.E.
- Contrail Suppression: Charlie Jackson at NASA Langley.
- Generic Low RCS Inlet Work: McAir. Charlie Jackson at NASA Langley, Glen Varney at G.E., Dave Migdal at P&W.

- Laser & Optical Air Data System: Lockheed. Perkin Elmer. Conventional Air Data mod for LO, Rosemount.
- High Temperature RAM: GE, [illegible], Vought Missiles, McDouglas Astro, L[illegible].
- SLAM: Dave Stegman is point of contact.
- Folding Fin HARM: HARM program office at China Lake. No point of contact yet.
- Integral Surface Treatment: GD, Boeing, Alcoa Def. systems.
- EF Emission Detection Systems: IBM (Nat H. will see soon -- more feedback after that visit).
- Bandpass Radome: Brunswick, Radant, TI.
- [REDACTED]: Sanders, GD/FW
- [REDACTED]: Sanders
- IR Windows: Battelle
- LPI Radar: Gerry Ingurski. Hughes
- Electronic Shutter: Radant. (Maybe more info later)
- IRST/FLIR: TI, Hughes, Ford, Westinghouse. Some information may be available from a China Lake cooperative test program with several system suppliers.
- Covert Communications: "N" (North?) Electronics Division. This is probably the McDonnell Electronic Div.

- LPI Radar Altimeters: Honeywell
- LO Electronically Scanned Arrays: TI and Westinghouse.

It is possible that some more information may come out later, but the timing is uncertain. We probably can't count on much before our proposal.

Keith

WCK-86-01

25 November 1986

Memo to: Bill Conly, Purchasing

From: W. C. Kennedy

Subject: Sole Source Justification for Lockheed

Reference: SOR #395461

The work described in the attached Statement of Work WCK-494-01 is critical to the success of [REDACTED] aircraft program. The prescribed work involves technical effort related both directly and indirectly [REDACTED].

Lockheed Corporation has considerable prior experience in the design, manufacture and maintenance [REDACTED]. Many of their design techniques and materials used to achieve low observability are unique in the industry. Lockheed possesses expertise in application [REDACTED] to all of the subsystems present on an aircraft.

Due to stringent program schedule restraints, General Dynamics does not have time to develop the full range of technical skills and materials necessary to produce an optimum aircraft design. For this reason, it is recommended that Lockheed Corporation be selected as the sole source to accomplish the necessary work.

/s/W. C. Kennedy
W. C. Kennedy
Senior Engineer

/s/F. P. Kirkland
F. P. Kirkland
Manager, Signature
Technology Integration

/s/J. P. Lamers
J. P. Lamers
Program Manager

[REDACTED]

1009505-87

RH-02.87

To: P. Farr/K. Jackson

From: P. Deam/A. Repovich

Subject: Model 21 Weight Control Plan

Enclosure: (1) F-15A Weight Control Program

[REDACTED] The purpose of this memo is to present the weight control plan proposed for the Model 21 program. The weight control plan is required to be submitted to the Navy 30 days after ATP. In order to meet this early report date, the weight control plan needs to be agreed on prior to ATP. Special issues discussed in this memo are:

- (U) Weight Savings Criterion
- (U) Weight Reserves
- (U) Target Weights
- (U) Weight Control Board

(U) The Model 21 will require a strong weight control program to meet the weight empty of our BAFO proposal. Major concerns which could lead to an overweight condition are:

- [REDACTED] Fixed Price contract
  - Cost will be big driver
- [REDACTED] Tight Schedule
  - Fewer Redesigns
  - Acceptance of Vendor Overweight
- [REDACTED] High Risk Items

- Basic Airfoil Structure
- Composites versus Aluminum
- Strike Bay System
- [REDACTED]
- E^3 Protection

(U) The proposed weight control plan uses the F-15A weight control plan (Enclosure 1) as the boilerplate for Model 21. The proposed weight control flow diagrams are shown in Figures 1A and 1B. Highlights of the weight control plan are:

- (U) Establishment of Target Weights
- (U) Monitoring
- (U) Visibility and Probability Analysis
- (U) Potential weight reductions
- (U) Timely Reports

(U) A procedure to present, review, evaluate, approve and disseminate configuration changes must be established and implemented as soon as possible to maintain weight control/status of the aircraft.

[REDACTED]

UNCLASSIFIED

/s/ DATE: 9/20/99
Thomas J. Payne

5 March 1987

MODEL 21
FOR THE UNITED STATES NAVY

[REDACTED]

I Executive Summary
Volume 1 Executive Summary (U)

[REDACTED]

MCDONNELL DOUGLAS
MCDONNELL AIRCRAFT COMPANY

GENERAL DYNAMICS
Fort Worth Division

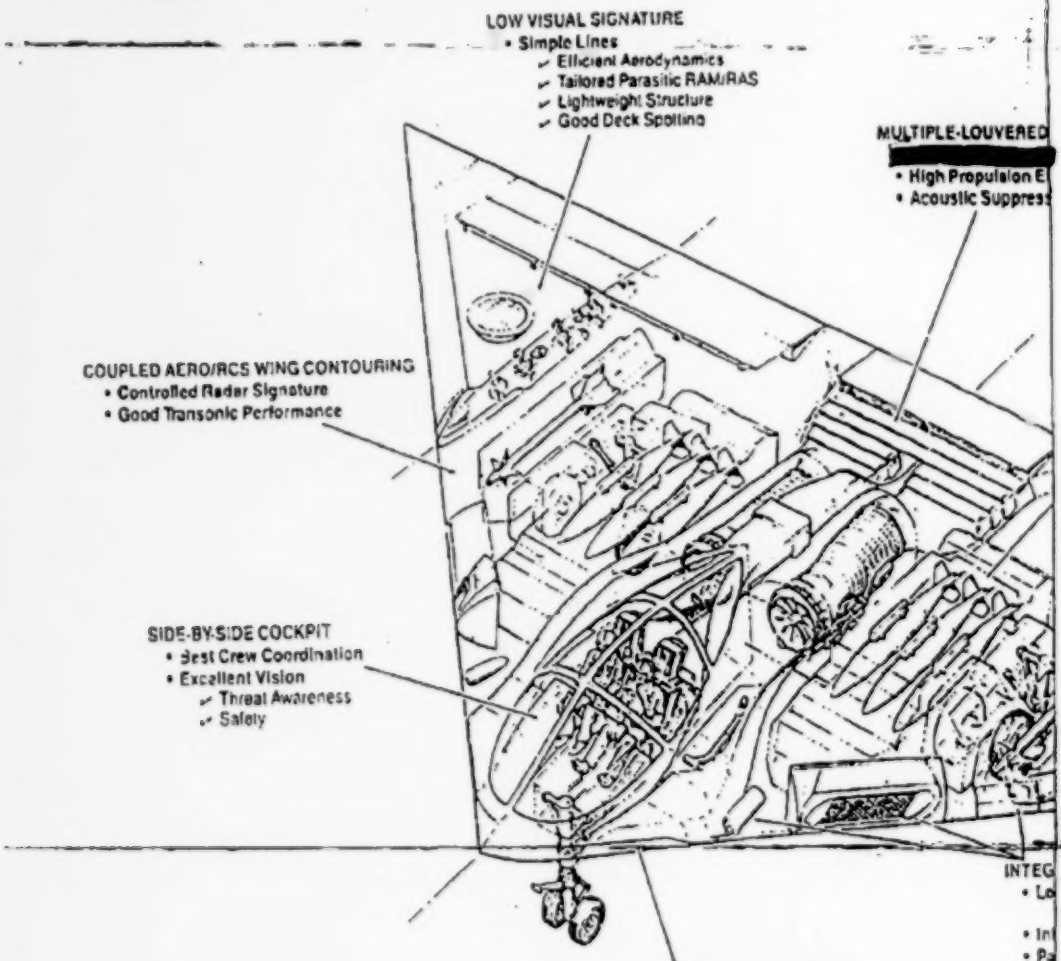
This proposal or quotation includes data that shall not be disclosed outside the Government and shall not be duplicated, used or disclosed - in whole or in part - for any purpose other than to evaluate this proposal or quotation. If, however, a contract is awarded to this offeror or quoter as a result of - or in connection with - the submission of this data, the Government shall have the right to duplicate, use, or disclose the data to the extent provided in the resulting contract. This restriction does not limit the Government's right to use information contained in this data if it is obtained from another source without restriction. The data subject to this restriction are contained herein.

[REDACTED]

OK MTW
OK TJP

[redacted]

Figure 1-2 [redacted] Model 21 — A Balanced, Combat-Effective Navy Medium-Attack Aircraft



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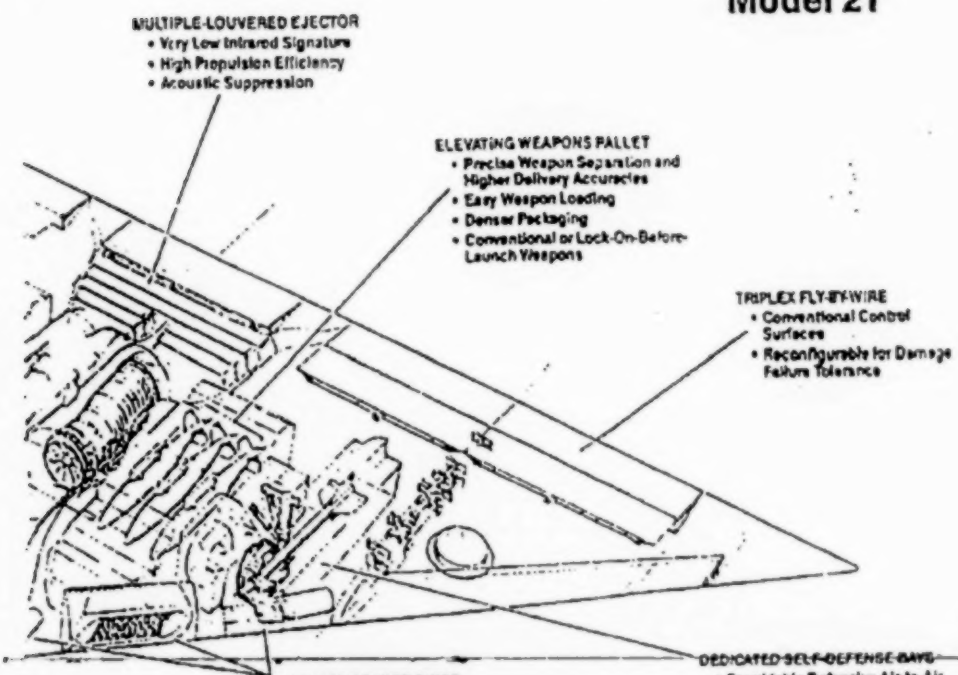
SECRET/NAOPH

McDonnell Douglas / General Dynamics

Model 21



...ACE INLETS
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[redacted]

APP. 87,193

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(U) Electromagnetic Emission Are Controlled

[REDACTED] Intentional and unintentional EM emission are managed to enhance survivability. Low-probability-of-intercept (LPI) modes of operation (spatial, power, and frequency manipulation) are employed. RF emission are minimized through highly integrated emission management techniques, emphasizing passive operation of systems and sensors in all mission phases.

[REDACTED] Multi-Company [REDACTED] Are Employed

[REDACTED] MCAIR and GDFW are industry leaders in developing and applying signature reduction technologies to operational tactical aircraft. Some notable examples are the Radar Target Scattering Facility, RATSCAT, which was designed, built and operated by GD; F-111, the first operational aircraft using Radar-Absorbing Material (RAM) and Radar-Absorbing Structure (RAS) and meeting an RCS Spec.; Gray Butte, site of [REDACTED] testing built and operated by MCAIR; Tomahawk and Advanced Cruise Missile, using LO [REDACTED] and other Special Access programs.

[REDACTED] In order to assure the [REDACTED] experience available, particularly in

the area of RCS, the MCAIR/GDFW team has utilized Lockheed and Rockwell International as subcontractors during the Dem/Val phase. This combined team has the total current operational experience on [REDACTED] aircraft. The final selection [REDACTED] concepts and components will be made from the four contractors' proposals, based upon both cost and performance benefits.

[REDACTED] Figure 1-6 shows Model 21 undergoing a portion of the 1000-plus hours of testing that have improved and validated its RCS characteristics. Figure 1-7 summarizes the multi-company, real world experience that reduces Model 21's operational RCS risk.

Figure 1-6 (u) Validated RCS Characteristics

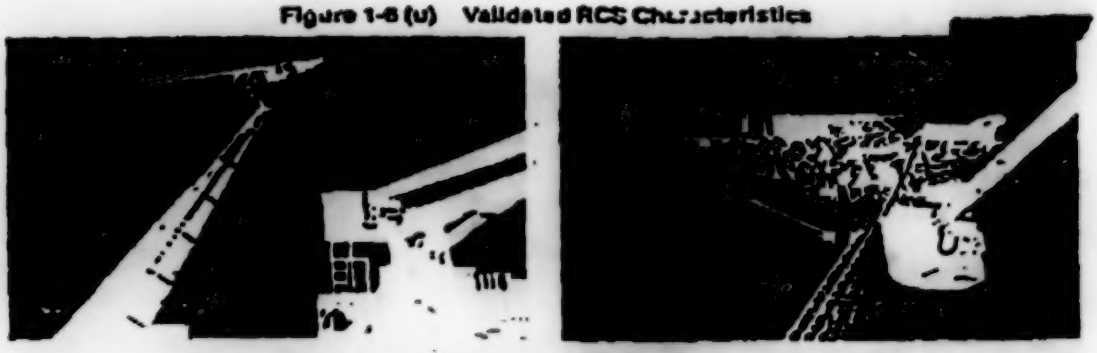
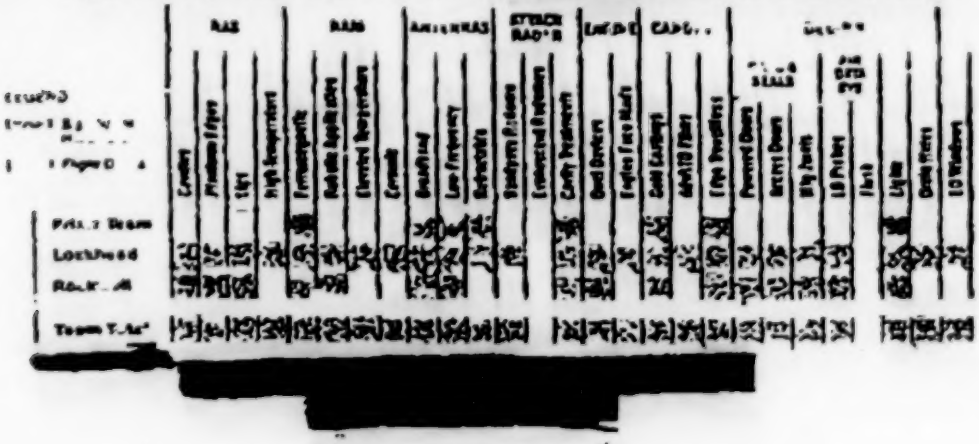


Figure 1-7 (u) Team and Subcontractor [redacted] Experience Minimizes Risk



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No. 91-1204C
(JUDGE HODGES)

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION
AND GENERAL DYNAMICS CORPORATION,

Plaintiffs,

V.

THE UNITED STATES,

Defendant.

APPENDIX TO DEFENDANT'S BRIEF REGARDING EFFECT OF STATE SECRETS AND MOTION FOR RECONSIDERATION
VOL II of IV

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Tele: (202) 514-7300

Dated: March 23, 2001

Attorneys for Defendant

PRELIMINARY [REDACTED]

NO: 208/5222/TD2078

DISCUSSION INFORMATION REQUEST

REQUESTOR: DUDLEY CATE/ ROGERS ENGLE (NAME & CODE)	DATE: 1 JUNE 1987
MEETING:	
REFERENCE:	II 5 (VOLUME/BOOK)
(PIR/SPEC/PROPOSAL)	COMPLETE (PARA./PAGE)
SUBJECT:	NAVAIR WEIGHT CONCERNS

QUESTION:

(U/[REDACTED] WHO IS THE "SINGLE-POINT-OF-CONTACT" FOR 200/208 REGARDING MASS PROPERTIES.

RESPONSE:

[REDACTED] Prior to ATP - Prior to ATP, Ross L. Williams, Building 206, Hello I, will serve as the single-point-of-contact.

[REDACTED] After ATP - Subsequent to ATP, a full-time element manager will be assigned to direct and control WBS Element 11CT Mass Properties and will also serve as a NAVAIR single-point-of-contact.

QUESTION:

(U [REDACTED] DO YOUR SUBCONTRACT PROCUREMENT SPECIFICATIONS CONTAIN "TEETH" (PENALTY CLAUSES) TO ENCOURAGE ACHIEVEMENT OF SPECIFIED WEIGHT GOALS?

RESPONSE:

(U [REDACTED] Our General Terms and conditions contain a very extensive warranty provision. This warranty covers both design and deliverables and requires the supplier to "meet or exceed the requirements contained in this contract". We consider all our specification and other requirements to be essential to meeting our customer's needs.

(U [REDACTED] Our suppliers are contractually bound to take all actions necessary to correct all deficiencies including redesign for performance breaches. An overweight item would require the supplier, as part of this warranty obligation, to redesign the offending item at his own cost. In addition, since design defects could be so critical to our performance, we have also placed a requirement to submit to us a plan for their corrective action within 60 days of the identification of an overweight condition. Upon the receipt of such a plan, we will follow our suppliers progress in correcting design defects.

[REDACTED]

QUESTION:

(U [REDACTED] ADDITIONAL INFORMATION IS REQUESTED REGARDING NAVAIR WEIGHT ASSESSMENT ISSUES.

RESPONSE:

(U [REDACTED] Our response is made on a one-for-one basis of each issue discussed. The issues and weight assessments are summarized in the following table and detailed discussions follow.

[REDACTED]

[REDACTED] NO: 208/5222/TD2078

(U) MODEL 21 WEIGHT EVALUATION SUMMARY

ISSUE	WEIGHT ASSESSMENT NAVAIR	RESPONSE
STRUCTURE	(1418)	(108)
COMPOSITE	900	0
ALLOWABLES		
COMPOSITE NCN-		0
OPTIMUM		
NUCLEAR	300	0
HARDENING		
BALLISTIC		0
VULNERABILITY		
LO	-	50
MAINTAINABILITY		
WING FOLD	-	38
MECHANISM		
BRAKE ENERGY	186	0
ARRESTING GEAR	-	20
MECH.		
OTHER	32	*
PROPULSION	(290)	(50)
ENGINE WEIGHT	151	0

AMAD WEIGHT	38	0
IFR DOOR LO PENALTIES	15	0
FUEL SYSTEM WEIGHT	83	50
OTHER	3	*
SYSTEMS	(1531)	(441)
FLIGHT CONTROL SENSORS	66	0
AFU STARTING AND INSTL.	84	23
SUBSYSTEM MONITORING	25	0
FUEL QUANTITY SYSTEM	34	22
HYDRAULIC FLUID WEIGHT	53	65
GENERATOR WEIGHT	80	0
FEEDER WIRE WEIGHT	60	0
K WEIGHT IMPACT	80	0
LO EXTERIOR LIGHTS	50	49
SUPPORTS -- ELECTRICAL	30	0
AVIONICS EQUIPMENT	419	159
AVIONICS INSTALLATION	312	56
AN/AWW - 13 PROVISIONS	52	0
ECS WEIGHT	111	67

OTHER	75	*
CONTINGENCY	(-500)	(0)
UNUSABLE FUEL	(70)	(70)
TOTAL WEIGHT CHANGE	2809	669

* NO RESPONSE, ISSUES NOT IDENTIFIED

15 September 1987

MODEL 21
FOR THE UNITED STATES NAVY

BAFO
IX PRICE REPORT
Volume 1.1 Price Proposal Summary(u)
and Appendix A and B

[REDACTED]

MCDONNELL DOUGLAS GENERAL DYNAMICS
MCDONNELL AIRCRAFT *Fort Worth Division*
COMPANY

This proposal or quotation includes data that shall not be disclosed outside the Government and shall not be duplicated, used or disclosed - in whole or in part - for any purpose other than to evaluate this proposal or quotation. If, however, a contract is awarded to this offeror or quoter as a result of - or in connection with - the submission of this data, the Government shall have the right to duplicate, use, or disclose the data to the extent provided in the resulting contract. This restriction does not limit the Government's right to use information contained in this data if it is obtained from another source without restriction. The data subject to this restriction are contained herein.

---

1 INTRODUCTION (U)

[REDACTED] The MCAIR/GDFW team welcomes the opportunity to propose this Fixed Price Incentive (FPI) Best and Final Offer (BAFO) for the Model 21 ATA program, which results in a target price and funding requirement lower than the stated USN objective. This lower target price includes the incorporation of an upgraded F404-F5D2 engine into the Model 21, as well as a number of additional RFP requirements such as instrumentation for another FSD aircraft and an enhanced Weapons System Trainer visual system. Under an FPI arrangement, our program, including these improvements, can be offered at a ceiling price equivalent to a firm fixed price proposal.

[REDACTED] Since our initial March 1987 submittal, we have gathered additional test data which confirmed our expectations in the Low Observables aspects of our design. We have further reviewed and, in the process, reaffirmed our weight and cost estimates. These factors, and our confidence in our design configuration, taken together with the dramatically improved performance margins afforded by inclusion of the F5D2 engine, have enabled us to confidently propose and accept a management challenge that results in a FSD target price well within the Navy's guidelines, with an attendant lower ceiling price.

[REDACTED] Additionally, based upon discussions with the Navy, we offer two alternate Model 21 configurations: a tandem crew station and an increased volume alternative. Detail

substantiation furnished in Volumes 1.3 and 1.4 of this report shows a relatively modest cost impact for these variants. MCAIR/GDFW are pleased to offer NAVAIR the choice of either or both of these alternates within the same FSD target and ceiling prices and for the same not-to-exceed Lot 1, 2, and 3 values as the baseline.

[REDACTED] Furthermore, the alternates can be offered to NAVAIR on the same aggressive schedule proposed for the baseline side-by-side configuration, which anticipates first flight at 30 months after program go-ahead, because we have already proceeded with the long lead and development intensive efforts for all configurations.

[REDACTED] Another result of our discussions with NAVAIR is reflected in the modified terms and conditions of this BAFO. We are deleting such previous conditions as business base variance adjustments, aggregation of the production lot not-to-exceed values, and the sharing arrangement for costs of retrofitting warranty changes. Further, we have removed the requirement for termination of extant contracts concurrent with program cancellation to ensure funds for tooling investment recovery. We have also increased the groupings of line items in the production

---

BAFO
IX Price Report
Volume 1.1

Figure 2-1. (U) Firm Program Value Summary*

[REDACTED]

Description	Quantity Aircraft	Program Value (Then Year Dollars In Millions)
Full Scale Development (1)	8	$ 4,379.2
Production Option 1	6	1,145.2
Production Option 2	8	1,306.5
Production Option 3	20	1.819.5
Subtotal	42	$ 8,650.4
Tooling Investment	-	321.4
Total	42	$ 8,971.4

Other Options

Description	Quantity Aircraft	Program Value (Then Year Dollars In Millions)
Option V - Refurbishment of FSD Aircraft	4	$ 280.2
Option VI - Technical Data Package	-	$ 1,368.3

Notes:
FPI target price of $4,379.2 M equates to USN $4,500 M objective. Using OSD factors $4,379.2 M de-escalates to $3,702.9 M in CFY 1985 dollars.
* Figure extensively revised

2.1 (U) Full Scale Development Pricing

[REDACTED] MCAIR/GDFW propose the following Fixed Price Incentive BAFO contract values for the Full Scale Development of the Model 21 aircraft.

[REDACTED] Figure 2-2 identifies the management challenge addressed in the introduction to this volume. MCAIR/GDFW are confident this challenge can be achieved due to the realistic estimating baseline of this BAFO coupled with the following additional factors:

a. [REDACTED] Full Scale Model 21 testing since our 30 March 1987 submittal has validated earlier full scale data, reducing technical, schedule, and cost uncertainties.

BAFO
IX Price Report
Volume 1.1

Figure 2-2. (U) Full Scale Development Pricing*

[REDACTED]

[HANDWRITING OMITTED]

	Full Scale Development BAFO Contract Values
Estimated Cost	$ 4,308,901,165
Management Challenge	(322,792,587)
Proposed Target Cost	$ 3,981,108,578
Target Profit	$ 398,110, 858
Target Price	$ 4,379,219,436
Ceiling Price (120% of Target Cost)	$ 4, 777,330,294

* New figure

b. **[REDACTED]** Incorporation of the improved thrust engines provide added margins in combined performance and carrier suitability. The core technology has been validated in the CE23A demonstrator program, thereby minimizing testing and risk associated with the GE F404/F5D2 engine.

c. **[REDACTED]** Our BAFO procurement cost estimates reflect extensive fixed price agreements with major suppliers, protecting against cost growth. At the same time, our conservative approach to meeting specification requirements should yield some opportunities to identify simpler, synergistic, or perhaps off-the-shelf solutions to achieve the specified parameters at reduced cost.

d. [REDACTED] The above margins and assurances will afford the team greater opportunity to focus on the design to cost (DTC) requirements of Addendum 637 to SD-8706C, thereby reducing FSD recurring aircraft cost with attendant production program benefits. As noted in Chapter 14 of the ILS-DS-30A-155, both DTC and Life Cycle Cost (LCC) will be used to manage program cost from the beginning of FSD.

e. [REDACTED] The MCAIR/GDFW technical and management team is in place and has the endorsement of strong corporate commitments. Combined with the Model 21 design stability and maturity, we expect a running start at go-ahead, which maximizes schedule efficiencies and reduces cost.

208/BRR/009281-87
TOTAL PAGES 31
COPY 1 OF 1 COPIES

[REDACTED]

WEIGHT REVIEWS
PRB 2 SEPT 87
AND
BAFO PERFORMANCE

THIS DOCUMENT HAS BEEN REVIEWED BY SECURITY AND IS TO BE HANDLED AND CONTROLLED AT THE UNCLASSIFIED LEVEL, DISREGARD CLASSIFICATION AND MARKING INSTRUCTIONS THAT DO NOT APPLY. THE RECLASSIFICATION/ DECLASSIFICATION APPROVAL OF THIS DOCUMENT IS BASED ON THE CURRENT A-12 SECURITY CLASSIFICATION GUIDELINES APPROVED BY OP-M59B

[REDACTED] SIGNATURE /s/

DATE 9/14/95

[REDACTED]

UNCLASSIFIED

STRONG WEIGHT CONTROL NEEDED

- FIXED PRICE CONTRACT
  - COST WILL BE BIG DRIVER
- TIGHT SCHEDULE
  - FEWER REDESIGNS

- ACCEPTANCE OF VENDOR OVERWEIGHT

- **HIGH RISK ITEMS**
  - BASIC AIRFOIL STRUCTURE
  - COMPOSITES vs ALUMINUM
  - STRIKE BAY SYSTEM
  - **[REDACTED]** TREATMENTS/DESIGNS
  - E^3 PROTECTION

[REDACTED]

1095

No. 91-1204C
(JUDGE HODGES)

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION
AND GENERAL DYNAMICS CORPORATION,

Plaintiffs,

V.

THE UNITED STATES,

Defendant.

APPENDIX TO DEFENDANT'S BRIEF REGARDING EFFECT OF STATE SECRETS AND MOTION FOR RECONSIDERATION
VOL III of IV

STUART E. SCHIFFER,
Deputy Assistant Attorney General

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Director

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Attn: Classification Unit
8th Floor
Washington, D.C. 20530
Tele: (202) 514-7300

Dated: March 28, 2001

Attorneys for Defendant

MEMO

Informal
13 June 1988

Subject: WEIGHT GROWTH CONCERN

To: Ed Bailey, Dick Pandorf, Glen Phariss, John Roche, Mark Thorpe, Ross Williams

CC: Pike Farr, John Havey, Hugo Heyns, John Hickle, Keith Jackson, Art Repovich

Enclosure: (1) Engineering Review on Heights

1. An "all hands" meeting for engineers was given Friday, 10 June 1988 to show our concern about the weight growth and the trend that is becoming apparent for the vehicle. The meeting's charts were presented in Enclosure (1).

2. Enclosure (1) is submitted for your use and reference. Engineers not attending the "all hands" should be made aware of our concern.

John H. Suchan

1098

10 JUNE 88

ENGINEERING REVIEW

WEIGHTS ARE GOING OUT OF CONTROL

NOSE LANDING GEAR	159#
MAIN LANDING GEAR	290#
INLET VANES	500#
PITCH FLAPS	125#
COMPOSITE MATERIAL	269#

WEIGHT ARE GUARANTEED

WEIGHT CONTROL IS CRITICAL

FOR 1000# INCREASE IN WEIGHT EMPTY

REQUIRES ADDITIONAL 250 LBS OF FUEL FOR EQUIVALENT MISSION RANGE

REQUIRES ADDITIONAL

2 KTS KNOTS W.O.D. LAUNCH

3 KTS KNOTS W.O.D. RECOVERY

ENGINEERING REVIEW

WHAT MUST BE DONE TO CONTROL WEIGHT INCREASE

- TIGER TEAMS
  - GOOD
  - EXAMPLE
    - BAY ACTUATOR AND DOOR
    - NOZZLE
  - CAN'T HANDLE ALL
- INDIVIDUAL EFFORT
  - IMPORTANT CONTRIBUTOR
  - TAKE INITIATIVE
    - REMOVE OVERLAPPING ASSUMPTIONS
    - ELIMINATE CONSERVATIVE GROUND RULES
    - OBTAIN SPEC. RELIEF
    - DESIGN TO ZERO MARGINS
    - CHALLENGE DESIGN
    - BRING IN EXPERTS
    - COMMUNICATE
- INCENTIVES

1100

ENGINEERING REVIEW

THINK WEIGHT

WEIGHT CONTROL

WEIGHT REDUCTION

IS CRITICAL

* * * * * * * * * * * * * * * *

UNCLASSIFIED

* * * * * * * * * * * * * * * *

CCO-05.08

5 July 1988

Memo to: Distribution

From: C. C. Olmsted

Subject: Minutes of GDFW Weight Control Board No. 2, 1 July 1988

Enclosures:
(1) WBC No. 2 Agenda
(2) Current Weight Breakdown by Manager
(3) Potential Weight Reduction Areas
(4) Design Review Schedule
(5) Fuel System and Pressure Data
(6) Minimum Thickness in Machined Parts
(7) Status Report #6 Increments

1. Attendees at the meeting were:

F. Auld	L. Fletcher	F. Olson
B. Beaty	S. Flores	G. Schumacher
L. Boddie	C. Fondon	L. Seth
D. Cox	M. Garrison	J. Shidler
S. Campbell	J. Gulley	B. Stout
P. Cleveland	C. Hice	B. Stribley
N. Damerau	K. Jackson	J. Suchan
P. Daniel	F. Kutzler	D. Uhl
J. Evans	S. Lopiano	W. Woodrey

A. Farrell C. Olmsted B. Zeterberg

2. Introduction

A. The meeting agenda (Enclosure (1)) was briefly discussed. The action items from WCB No. 1 are included in this meeting's agenda. One open item was reassigned.

ACTION: (G. Evans) Set up schedule for "Importance of Weight Meetings"

B. The other open item "Structural Design Temperatures (Woodrey/Lee) will be discussed at an upcoming WBC meeting.

3. Best Guess Current Weight Summary

A. A Weight Summary of the current best estimate versus BAFO weight was presented. The current best estimate is 3523 lb. over the BAFO guaranteed weight empty. This increase is broken down as follows:

		Delta Weight (6-25-88)
Structure		2588
N	1151	
S	1437	
Systems		916

	1103	
N	433	
S	483	
Exterior		519
N	80	
S	493	
Contingency		-500

This overweight condition MUST be remedied and the task to get the weight out falls on EVERYBODY. This aircraft must perform its primary functions but cannot and will not have any "Gold Plated" extras. Schedule changes will be considered if the overweight can be removed as a result of more time being available to solve the weight related problems.

B. Detail support data, by manager and group leader, that details the over weight problem as presented is contained in Enclosure (2).

* * * * * * * * * * * * * * * *

UNCLASSIFIED

* * * * * * * * * * * * * * * *

1104

GENERAL DYNAMICS
Fort Worth Division

Date: 15 August 1988
To: Pat Hogan
From: JAMES C. MIFSUD
Subject: PDA between General Dynamics, McDonnell-Douglas and Northrop

Attached are three originals of the subject agreement which have been executed by the Legal Department.

Please have the points of contact filled in by McDonnell-Douglas and Northrop upon execution.

Please return one fully executed original to me for our files.

NOTE: No information is to be released pursuant to this PDA until all parties have executed the agreement.

James C. Mifsud

JCM:ht
Attachments

PROPRIETARY DATA AGREEMENT

This Agreement is entered into by and between the following parties: McDonnell-Douglas Corporation, a corporation of Maryland, McDonnell-Douglas Aircraft Company having an office at St. Louis, Missouri (hereinafter referred to as "McDonnell Douglas"), and Northrop Corporation, a corporation of Delaware, Northrop Aircraft Group having an office at Hawthorne, California (hereinafter referred to as), and General Dynamics Corporation, a corporation of Delaware, through its Fort Worth Division, having an office at Fort Worth, Texas (hereinafter referred to as "General Dynamics").

SUBJECT: Cross-Program Briefing on A-12 and B-2 Aircraft

WHEREAS, with respect to the "Subject" above, each party represents that it now has, or may in the future develop or acquire, certain ideas, concepts, information or data, some of which (including data of others for whom it may be acting) may be considered by the respective party as its proprietary or competition-sensitive data or information (hereinafter referred to as "Proprietary Data"), as follows:

Proprietary Data of: Northrup: Data or information concerning Northrop's B-2 Airdata system.

Proprietary Data of: McDonnell-Douglas: Programmatic data concerning McDonnell-Douglas/General Dynamics A-12 Aircraft including

performance characteristics of the aircraft, but excluding delivery, production and cost information.

Proprietary Data of: General Dynamics: Programmatic data concerning McDonnell-Douglas/General Dynamics A-12 aircraft including performance characteristics of the aircraft, but excluding delivery, production and cost information.

WHEREAS, General Dynamics and McDonnell-Douglas possess certain Proprietary Data relating to the A-12 System which might be of benefit to development of the B-12 System, and Northrop possesses certain Proprietary Data relating to the B-2 System which might be of benefit to development of the A-12 System, and

WHEREAS, the parties for their mutual benefit and at the specific request of the Naval Air Systems Command, desire to disclose to one another, upon receipt of Contracting Agency approval, such Proprietary Data;

NOW, THEREFORE, in consideration of the premises and the mutual covenants contained herein, the parties agree as follows:

1. This Agreement provides only for the handling and protecting of Proprietary Data and shall not be construed as a Teaming, Joint Venture, or other such arrangement.

2. During the term of this Agreement, the parties hereto, to the extent of their right to do so, may exchange Proprietary Data. However, no party has an obligation to supply Proprietary Data hereunder.

3. Proprietary Data shall be delivered by the disclosing party to the receiving party in writing or other tangible form at the time of disclosure and prominently identified on the face thereof by the disclosing party as proprietary by appropriate legend, stamp or other marking. Any party hereto receiving Proprietary Data pursuant to this Agreement is authorized to supply such data to any other party to this Agreement provided the Proprietary Data supplied bears all of the restrictive markings appearing on the data as originally received from such party supplier. *No data not in fact* proprietary to the disclosing party (or to another for which the party is acting) shall be so claimed or so marked, and the parties shall endeavor to keep to a minimum the amount of Proprietary Data disclosed hereunder.

4. Each party shall take reasonable steps to preserve the Proprietary Data received pursuant to this Agreement, and identified as in the preceding paragraph, from disclosure and dissemination to third parties. The parties shall be deemed to discharge their entire obligation hereunder if they use the same degree of care to safeguard the Proprietary Data received as they normally use to safeguard their own similar Proprietary Data in similar circumstances. McDonnell-Douglas and General Dynamics shall use Proprietary Data received from Northrop only in support o the A-12 Program. Northrop shall use Proprietary Data received from General Dynamics or McDonnell-Douglas only in support of the B-2 Program. Inasmuch as General Dynamics is currently

competing against McDonnell-Douglas and Northrop for award of the Advanced Tactical Fighter (ATF) Full Scale Development Contract, the Parties, in accordance with the stipulations contained herein, shall not use Proprietary Data received pursuant to this Agreement in support of their respective ATF Programs.

5. Verbal disclosures of Proprietary Data will be protected as set forth in this Agreement for written disclosure provided that at the time of first verbal disclosure to the party receiving the data:

a. the disclosing party makes clear to the receiving party the proprietary nature of the data,

b. written notation is made of the Proprietary Data, and

c. The disclosing party confirms the verbal disclosure by transmitting the Proprietary Data in written form (identified and marked as in numbered paragraph 3. above) to the receiving party within ten (10) calendar days following said first verbal disclosure.

6. Notwithstanding the restrictions above with respect to disclosure of Proprietary Data to third parties, the parties may incorporate such Proprietary Data in a proposal, report, or other submittal to the U.S. Government provided the data disclosed to the Government bears legends in accordance with Attachment "A" hereto.

7. No party shall be liable to the other for disclosure of any Proprietary Data if the same:

a. is not identified as proprietary in accordance with this Agreement, or

b. is disclosed by either party after 5 year(s) from the date of receipt of such Proprietary Data, or

c. is now in or hereafter comes into the public domain without breach of this Agreement, or

d. is known to the receiving party prior to disclosure by the disclosing party, or

e. bears a notice of copyright, or

f. is independently developed by the receiving party, or

g. is disclosed by the receiving party with the written approval of the disclosing party, or

h. is disclosed by accident, inadvertence or mistake, or

i. becomes known, without breach of this Agreement, to the receiving party without like restrictions to those herein, or

j. is disclosed by the disclosing party to a third party without

restrictions similar to those in this Agreement.

8. Primary but non-exclusive points of contact for the transmission and control of Proprietary Data exchanged hereunder, are:

For McDonnell-Douglas

For Northrop

For General Dynamics
S. K. Jackson
A-12 Deputy Program Director
General Dynamics Corporation
Fort Worth Division
P.O. Box 748, M2 5986
Fort Worth, TX 76101

Each party may change its primary point of contact by written notice to the other parties.

9. Neither the execution and delivery of this Agreement nor the delivery of any Proprietary Data hereunder shall be construed as granting either expressly or by implication, estoppel or otherwise, any right in or license under any present or future data, drawings, plans, ideas or methods disclosed under this Agreement, or under any invention or patent now or hereafter owned or controlled by any party hereto.

10. This Agreement may be terminated with respect to any party by such party giving thirty (30) days written notice to the other parties, and,

unless sooner terminated, shall automatically terminate 1 year(s) from the effective date hereof. However, such party's obligation to protect previously received Proprietary Data shall survive any such termination, subject to the limitations specified elsewhere in this Agreement.

11. This Agreement shall be governed by and interpreted in accordance with the law of the State of Texas.

12. This Agreement contains the entire understanding relative to the protection of Proprietary Data and supersedes all prior and collateral communication, reports, and understanding, if any, between the parties. No modification or addition to any provision hereof shall be binding unless in writing and signed by the parties. This Agreement shall apply in lieu of and notwithstanding any specific terms contained in any legend or statement associated with any particular Proprietary Data exchanged, and the duties of the parties shall be determined exclusively by the terms and conditions herein.

13. This Agreement may be modified in any respect at any time by a writing signed by all parties.

14. This Agreement shall be effective when executed by all parties.

15. This Agreement shall be executed in three counterparts, each of which shall for all purposes be deemed an original.

McDonnell Douglas Corporation
McDonnell-Douglas Aircraft Co.

By
Name
Title
Date

GENERAL DYNAMICS CORPORATION
Fort Worth Division

By /s/ E.O. Brown III
Name E.O. Brown III
Title Assistant General Counsel
Date 15 August 1988

Northrop Corporation

By
Name
Title
Date

MEMO

Informal
30 August 1988

Subject: INFORMATION ON THE B-2 AIRCRAFT TO BE PROVIDED TO THE A-12 PROGRAM

To: E. Bailey, J. Bogdanor, A. Borchers, N. Martens. R. Pandorf, G. Phariss, P. Reger, J. Roche, J. Suchan, M. Thorpe, R. Williams, G. Woodson, J. Wynne

CC: J. Tyson, H. Snodgrass

1. The enclosed items were requested and will be discussed at least with Keith and myself on 13 September in Dayton.

2. This list is *highly* sensitive and should be provided only to those people who have a need to know.

A. P. Farr

1. Low Observable Air Data System
   - o Including anti-ice criteria & systems
2. Low Observable Components
   - o Concept descriptions and, where applicable, qualified suppliers.

   Examples:

   - Door seals
   - Control surface seals
   - Fasteners
   - Latches - structural/ quick release
   - Vent and drain holes
   - Lights
   - Antennas
   - Canopy coatings & attachments concepts
   - Crack & gap treatments & tolerances
   - Surface smoothness criteria
   - EO window treatment types

3. Elevated temperature RAM/RAS materials and structural design concepts

   - [REDACTED]
   - [REDACTED]

4. Buckling – Critical composite structure design/manufacturing concepts
5. PAS material characteristics

   - 250° & below
   - R-card integration techniques

6. Maintainability
    - RAS repair & verification techniques
    - Repair criteria for surface smoothness
    - Spec engine removal time
7. Contrail Suppression
8. Signature specification & accounting process
9. LO compatible countermeasures including **[REDACTED]**
10. Non-metallic electrical connectors
11. Fire suppression techniques
    - Dry bays
12. Bay acoustic environment
13. Lightning strike data/analysis
14. Operational security & ILS security
15. Lessons learned

INTEROFFICE MEMORANDUM

Date: 12-May 1988 04:43pm CDT
From: John P. Lamers – FW
LAMERS, JP

Dept:

TO: Charles A. Anderson – FW (ANDERSON,CA)

Subject: Lockheed Termination

Today I directed my people to discontinue their efforts to forge a satisfactory arrangement with Lockheed.

Reasons are as follows:

- Marginal technical benefit
- 14 major terms/conditions issues of which three are show stoppers
- Out of bed $20M on cost
- Inability to achieve a satisfactory security posture.

No appreciable progress has been made in recent weeks on the foregoing items. Our backs are to the wall on schedule. Accordingly, we must move ahead with alternate plans.

I have a call in to Brizendine to inform him.

John P. Lamers

MEMORANDUM OF UNDERSTANDING FOR TECHNICAL TRANSFER BETWEEN B-2 AND A-12 PROGRAMS

1. THE PURPOSE OF THIS MEMORANDUM OF UNDERSTANDING IS TO ALLOW FOR AND FOSTER A TWO-WAY INTERCHANGE OF TECHNICAL INFORMATION BETWEEN THE B-2 PROGRAM AND THE A-12 PROGRAM. THIS INTERCHANGE IS TO PROVIDE LESSONS LEARNED AND POTENTIAL PROBLEM SOLUTIONS FROM ONE PROGRAM TO ANOTHER.

2. THEREFORE, IN THAT REGARD, TECHNOLOGY TRANSFER MEETINGS SHALL BE HELD AT NORTHROP B-2 DIVISION AND GENERAL DYNAMICS FORT WORTH A-12 FACILITY. AN INTERCHANGE MEETING WILL BE HELD AT GENERAL DYNAMICS FORT WORTH A-12 FACILITY ON 13 FEBRUARY 1990 AND ANOTHER INTERCHANGE MEETING WILL BE HELD AT NORTHROP B-2 DIVISION ON 28 FEBRUARY 1990. THESE MEETINGS WILL BE HELD AT LEVEL IV TO INSURE THE FREE FLOW OF CRITICAL TECHNICAL INFORMATION. THE SYSTEM PROGRAM OFFICE FOR EACH SYSTEM WILL ENSURE THAT ONLY CRITICAL ESSENTIAL PERSONNEL, BOTH GOVERNMENT AND CONTRACTOR, SUPPORT THIS INITIATIVE AND ARE BRIEFED LEVEL IV.

3. ANY FUTURE FOLLOW-UP MEETINGS WILL BE AS MUTUALLY AGREED TO BY THE UNDERSIGNED.

RICH. M. SCOFIELD,
MAJ GEN, USAF
PROGRAM DIRECTOR
B-2 SPO

L. G. ELBERFELD,
CAPT, USN
A-12 PROGRAM MANAGER
NAVAL AIR SYSTEMS
COMMAND

EDWARD SMITH
VICE PRESIDENT,
GENERAL MANAGER
NORTHROP A-2 DIVISION

JOHN P. LAMERS, VICE
PRESIDENT A-12 PROGRAM
DIRECTOR
GENERAL DYNAMICS,
FT. WORTH DIVISION

HARRY E.
SNODGRASS, VICE
PRESIDENT, GENERAL
MANAGER
MCDONNELL AIRCRAFT
COMPANY

COMPETITION SENSITIVE

06 September 1991

COMPARISON OF A-12 PROPOSALS

The target and ceiling prices for full scale engineering development (FSED) of an A-12 aircraft offered by GDC/McAir and Northrop/Grumman/LTV are highlighted in attachment (1). A difference between the ceiling prices of over $1.1 billion is shown. The difference in target price is substantially less totaling $563 million. These differences reflect not only variations in the development effort projected by the offerors', but also the price impacts of the offerors' teaming arrangements, inflation rates used, and their approaches to risk sharing between themselves and the government. A realistic understanding of the scope of effort, and consistency in cost and profit between bids can be gained by a review of the cost analysis completed during the A-12 competition. This review will show a difference in development effort projected that is less than $100 million dollars as bid by the two competitors; and based upon Navy estimates for both FSED proposals, is less than $305 million in then year dollars when the Northrop/Grumman/LTV proposal is adjusted upward to reflect a development program compliant to Navy Specifications.

[Bid Development Effort]

The difference in target prices was the more significant comparison as the target prices offered reflect each offeror's build-up of its development program including labor, materials, sub-contractor

costs to complete; all of the analyses, engineering design effort, ground test, and flight testing required in a full scale development program for a tactical military aircraft. The difference of $563 million dollars in target price shown on attachment opposed to differences in development effort required or underbidding on the part of one of the offerors. Northrop's a teaming arrangement treated Grumman and LTV as subcontractors and Northrop material overhead allowance, G&A, profit and other incidental add-ons were applied to the cost of that portion of the development program to be executed by LTV and Grumman. This amount shown on attachment (2) totals $487 million dollars and represents a prime contractor "handling charge" that is not accumulated on the comparable work in the winning GDC/McAir proposal. Since the GDC/McAir teaming arrangement made them, in essence, equal prime contractors, this significant "handling charge" was not present. When this amount is subtracted out of the difference in target prices, the remainder is $76 million dollars. Thus, the difference in pure development effort proposed by the two offerors' is less than $100 million dollars when a teaming arrangement similar to GDC/McAir is assumed for the Northrop/Grumman/LTV bid.

[Navy Independent Estimates]

Independent estimates of the full scale development price were developed by the Navy during the competition. Those comparisons are summarized and highlighted in attachment (3). Constant FY 85 dollars are used to remove the

effects of differing assumptions about inflation. The Navy's estimate in constant FY 85 dollars for the GDC/McAir proposal is $4.575 billion dollars and for the proposal submitted by Northrop/Grumman/LTV is $4.339 billion dollars. Here, we see the Navy's independent estimates projecting a higher price for the GDC/McAir bid. However, there were significant deficiencies in total flight test hours and other test deferrals in the Northrop/Grumman/LTV bid. When those were taken into account, the full scale development effort required to be completed increased raising the price projected by the Navy to $4.858 billion dollars. Thus, a difference between offerors of $283 million dollars was protected by the Navy when the Northrop/Grumman/LTV proposal was adjusted for compliance with our specifications. (The Northrop offer was higher.) The difference in projected target price was reasonable and consistent with differences between the aircraft configurations proposed and the details of the offerors' development plans and teaming arrangements.

The larger difference in ceiling prices resulted from a more favorable (to the government) share ratio bid by the GDC/McAir team if the development effort required to complete the contract became greater than estimated in their target price. Selection of a share ratio and resulting ceiling price are influenced by a variety of company subjective factors beyond the more pure development effort reflected in the FSED target price. Differences in factors such as proposed share ratios, risk allocation within the teams, profit, the company's financial health, a cushion to soften any developmental risk,

and simple competitive strategy are commonly factored into proposed FSED ceiling prices, which can, and most likely did in this instance, result in wide variations in FSED ceiling prices.

Attachment (1) also shows significant differences between not-to-exceed (NTEs) prices for the production options. These differences also are primarily the result of different bidding strategies between the competitors rather than an unyielding difference in the projected costs of manufacturing in the two offerors' proposals. Attachment (4) compares Navy developed estimates for production lot NTEs. These are based upon an analysis of the offerors' estimated production costs with aircraft characteristics based upon the Navy estimated weights for the respective aircraft. The differences between production NTEs are much less than those bid by the offerors'. Normally, we see a NTE approximately 30% or so higher than the projected cost of producing the item. In the case of the Northrop/Grumman/LTV proposal, the NTEs were around 74% higher than projected price (not projected cost) whereas the GDC/McAir offer was only around 12% higher than the projected cost. Thus, we concluded that the offerors' projected production costs were consistent, and the large difference in production prices bid reflected a very large cushion built into the Northrop/Grumman/LTV bid. The reasons for that cushion were not clear from an analysis of their proposal nor an identification of unusual manufacturing risk in the proposal.

A further analysis for consistency in production cost estimates was accomplished and those results are summarized on attachments (5) and (6). There, we estimated production costs for an 850 aircraft buy quantity for each offeror. We projected a unit procurement cost difference of about $5 million dollars or roughly ten percent. In attachment (6) we further analyzed consistency between the offerors' recurring production cost estimates for the 850 aircraft buy. Starting with the Northrop/Grumman/LTV airframe recurring average of $28.2 million dollars and removing the handling charges for the type of contractor/sub-contractor relationship vice the winning bid reduced the estimated average to $25 million dollars. Next, we adjusted that projection by pricing the winning aircraft configuration which was smaller reducing the Northrop/Grumman/LTV recurring production price to about $20.4 million dollars. If we then take the winning offerors' baseline configuration and production estimate with a $17.7 million dollars airframe recurring average, and recomputed its price with the labor rates of the Northrop/Grumman/LTV team, we have a recurring average of $19.9 million dollars. Thus, we find a recurring price difference of approximately five percent.

Therefore, we concluded that a realistic pricing basis existed for both the program development cost estimate, and the production NTEs bid by the winning team. This analysis was briefed to the Cost Analysis Improvement Group in OSD prior to FSD contract go-ahead.

No. 91-1204C
(JUDGE HODGES)

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION
AND GENERAL DYNAMICS CORPORATION,

Plaintiffs,

V.

THE UNITED STATES,

Defendant.

APPENDIX TO DEFENDANT'S BRIEF REGARDING EFFECT OF STATE SECRETS AND MOTION FOR RECONSIDERATION
VOL IV of IV

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Tele. (202) 514-7300

Dated: March 28, 2001

Attorneys for Defendant

Page 7

Q. It appears you signed this document for John Lamers.
A. Yes, it looks like I did.
Q. If you look at the letter, which . . . . . appears to be headed "To Sam Sayers," Sam Sayers was program manager?
A. That's correct, Navy program manager.
Q. The letter indicates that it's providing the recommended master program plan, and that's apparently dated May 28, 1985.
A. That's correct.
Q. Were you involved in the development of this plan?
A. I was not involved in any great detail. I did consult with the people on this to some degree.
Q. But if there was a significant decision being made, like for example what the amount of time to first flight would be, that's something you would have known about for planning purposes?
A. I did know about those for planning purposes in general.
Q. If you turn to page 1830.
A. Okay.

Page 8

Q. And this appears to be the recommended MCAIR and GD master program

schedule as of May 28, 1985; is that your understanding?
A. That's what it looks like to me.
Q. If you look up at the top at, I guess I would call it, the actual first line of arrows as you move across, if you look at about September-October of 1987 –
A. Okay.
Q. – you see it says "ATP for FSD."?
A. Yes.
Q. And then if you move across 1988, it's broken down into months, and then 1989 [illegible] into quarters. Then it says "first [illegible] FSD aircraft" in what looks like the fourth quarter of 1989; is that how you'd read that?
A. That looks like, yes, fourth quarter of '89.
Q. And do you recall that in the spring of 1985 the recommended master program schedule for GD and MCAIR was recommending a 27-month path to first flight, from authorization to proceed until first flight?

Page 9

A. I did not recall that. At this stage, we discussed very many different times to first flight. I did not recall the 27-month.
Q. What are the ones that you do recall?
A. We discussed them all the way from about 40, 46. As I remember, normally it ranged between about 46 and 30, maybe a

little
bit less than 30. But my memory says about 30
was the lower end and about 46 was the high end.
This one obviously was a little
shorter than that.
Q. Do you recall at what point you were recommending paths to first flight in the 46-month
range?
A. Well, from my perspective – you mean as far as the companies were concerned? Well,
I don't think that we ever actually sent a schedule out that had a first flight schedule that long. This was internal discussions.
There were differences of opinion as
to what the schedule should be.
Q. And what was your opinion in that [illegible]?

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A. I typically was on the longer end of things
Q. Why was that?
A. It was a qualitative evaluation of what I saw as the time required to get closure on technical decisions.
Q. What's your recollection as of May of 1985 as to who would have been providing input
to this recommended master program schedule?

A. Well, of course probably the primary input came from program management. Harry Snodgrass in particular was, I think, very influential on this.
Q. And who else?
A. Well, of course some of the scheduling community worked on the schedules, although in general the program, major program milestones and schedule increments and so forth tended to be set by program management, so Harry Snodgrass and John Lamers and the respective managements of the different companies consulted on that.
Q. So when you say "scheduling community," are you talking about people like Frank Field and Marshall Grayson?

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A. Marshall Grayson was not in that.
Q. Frank Field?
A. McGiveny. I think Field was probably involved in it from MCAIR's side. I think McGiveny – is that his name? – from Fort Worth was a scheduler.
Q. And your recollection is they were the major players in 1985?
A. Yes. Boy, that's a long time ago now.
Let's see. That's my recollection. I'm fuzzy on exactly who's involved in that

time period.
Q. But your recollection is that determining the number of months to first flight, that's something that program management was setting?
A. Program management was setting that, and schedulers would also set it based on history, basically, what previous history had been primarily.
Q. Is it – sorry, go ahead.
A. Most of the scheduling operations work on what's been done in the past.
Q. Is it your recollection that in the

Page 12

period before the FSD contract that the people that were seeing these schedules were planning to have schedules that were more compressed or more conservative or relaxed than what a prior history was for an aircraft?
A. Well, in general I think that the schedules that people were setting at that time tended to be about the same and within the same time span as past aircraft. For example, I think the 27 months is about what the F-111 was, maybe a little longer than what the F-111 was, probably a little shorter than what the F-15 was, in the same ballpark, plus or minus two or three months, what the F-16 was.
So they were in the same ballpark.
Q. Was it your feeling at the time, say

1985, 1986, that the development of this aircraft could be done in about the same time as the F-111 or the F-15?

A. My personal opinion was I thought it would take a little longer than that. But I did not have any – this was based on my own view of technical factors.

My view was longer than what history

Page 73
or during FSD with regard to the A-12?
Is it your understanding that GD
maintained any proprietary rights to any of
that information?
MR. CHURCHILL: Again, you're calling
for a legal conclusion.
THE WITNESS: Yes. Yes, I'm not the
right person to talk to on that.
BY MR. SCHOONER:
Q. Well, other than the fact that your
counsel's given you some suggestions as to
how
to respond, I'm just asking what your
understanding is.
MR. CHURCHILL: He made the point about
not
being a legal expert before I even
objected, so it wasn't anything that counsel
had to tell him. It's the impropriety of your
question.
THE WITNESS: Again, that's a very
complex – at this stage the A-12 was a very
complex program. It went through two
stages.
When Lockheed bought the General Dynamics
Fort
Worth Division from General Dynamics, then
some of those went over to the AX program,
Page 74
which I was not involved with. And there

were
(2) teaming agreements with MCAIR on that.
(3) I think MCAIR wound up with the
(4) leadership on that aspect of it at one time.
(5) It was a very complex relationship and I
(6) frankly simply do not have any idea how the
(7) legal rights to that data – who owns those
(8) and what the status of that is. I think it's
(9) been an argument with the Government over
(10) rights in general.
(11) BY MR. SCHOONER:
(12) Q. Do you recall the first time there
(13) were any discussions between GD or MCAIR and
(14) Northrop with regard to possible subcontract
(15) relationship?
(16) A. Would you ask the question again?
(17) Q. Do you recall when the first time was
(18) that there were any discussions with GD or
(19) MCAIR and Northrop about a potential
(20) subcontract relationship?
(21) A. Oh, the first time I remember
(22) discussing exchanging technologies or talking
(23) about subcontractor relationships with respect
(24) to B-2 technologies was in early 1990, first
(25) quarter probably of 1990. Those were
Page 75
(1) primarily verbal discussions.
(2) I think other parts of Northrop had
(3) some other classified technology programs that
(4) they had briefed to us to be used on A-12. I
(5) can't remember when that was. I won't

mention
what that is right now because I think the program may still be classified.
Q. You mentioned exchanging technologies and subcontracting in the same sentence. What's your understanding about the difference between those two types of events?
A. Go back and repeat the question again, so I'm sure I have it;
Q. You mentioned exchanging technologies with Northrop and then subcontracting. What's the difference between those two, in your understanding?
A. Well, when we talk about a technology exchange, I'll describe what that was. We briefed Northrop on the A-12 concept as to what the airplane looked like, what kind of performance it had, what kind of signature levels it had, how it operated, what some of the technical challenges were, and where we stood on the program.

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Then Northrop reciprocated with a similar briefing to us on the B-2 as to similar kinds of things: where they were on the program, what their experiences were, what technology they had developed, so that we could understand what was available for both companies.
Then there were mutual discussions

about things that we had that Northrop could use and things that Northrop had that we could use. We had a couple of subsequent meetings and I think were just about to get to the point where we may have been able to make some – on a subcontract, then, we would have decided the specific technology that Northrop has, or vice versa, that we think can be of benefit to the A-12. The subcontract would be when you actually sign a contract to provide them funds to go provide you the hardware or whatever it was that you were contracting for.

Q. Now, when you talk about this reciprocation or this exchange, is that basically a trade of information as you understood it?

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A. Basically.

Q. And it's your understanding that that's different from a subcontract, in that in the subcontract one party gives money to the other party –

A. Right.

Q. – in exchange for information or goods or service?

A. Right, right.

Q. Was it your understanding that in this exchange of technology with Northrop that

you providing information to Northrop was a condition upon which they provided information to you?

A. It was at least an informal quid pro quo.

Q. Is it your recollection that before that exchange of technology there was never a time where GD or MCAIR approached Northrop about being a subcontractor?

A. I frankly do not have a recollection of that. I was not involved in all of the subcontracting activities and where our procurement people went to. I would be kind of surprised if at some point in time our

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procurement people did not approach Northrop for something, because we literally had out tens of thousands of procurement packages.

Q. Do you recall at the time the MCAIR and GD received the A-12 FSD contract that there was any discussion about approaching Northrop at that point to subcontract for A-12 work?

A. I don't remember any discussions on A-12 subcontract work, although there could possibly have been. I don't personally remember any at this date.

Q. Do you recall anyone advocating or suggesting that someone commence such an approach?

A. I don't personally remember that at this stage.
Q. Can you think of any reason why, when GD and MCAIR received the A-12 FSD contract, they wouldn't have proceeded to approach Northrop about a subcontracting arrangement?
A. Nothing specific, except that Northrop had been the main competitor on the contract. That would not necessarily have ruled out using them for something, however,

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we had had some of the F-117 information earlier in the program, it may have helped some.
By 1989, as far along as we were in the program, we didn't see a whole lot that we thought would be of great benefit. At least, as I said, we didn't get an in-depth technical briefing, but from what we saw it did not look like there was a great deal of information that we could have employed at that time in terms of impacting the airplane.
There was some interesting information on maintenance problems and operational issues that would have been valuable later, later on in that phase of the program.
Q. But your impression was that by the

summer of 1989 when you saw the F-117 that Lockheed had nothing to offer you that was going to help you get to first flight or help you get to FSD?
A. Right. I wouldn't say absolutely nothing. That's very all-inclusive. But almost nothing.

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Q. Do you ever recall Lockheed approaching you to have any kind of technology exchange, saying, we hear you have some technology, is there anything we can offer you?
A. I don't remember that specifically, although I do remember vaguely that we did talk to some of the Lockheed people at one occasion on some of the hot exhaust materials and that we did have some exchanges on that. And I'm not sure when that was. Some time during the program. That's the only thing specific I remember about that.
Q. Do you recall if that was F-117-related?
A. I did not know enough about what the F-117 had to know. The materials that we were using were Space Shuttle tile-derived materials.
Q. Is that like the tile that Rockwell was –
A. I think Lockheed probably supplied the tile for the Space Shuttle to Rockwell, and we were using materials derived from

that.
(24) The Skunk Works may have used that same kind
(25) of material on F-117, but we were not
Page 171
(1) knowledgeable enough to know where that was.
(2) We had people – nobody was briefed
(3) on F-117 except for that very brief period
(4) that a few of us went out there. So for most
(5) of the time, we had very little idea what was
(6) available on the F-117 or not available. We
(7) couldn't talk about it if it were.
(8) Q. And it's your recollection that when you
(9) were talking to Lockheed about the thermal
(10) barrier tile – is that the correct term?
(11) A. Yes, it's the thermal barrier tile.
(12) Q. And is that for, for example, the
(13) pitch flap region?
(14) A. This would be used for the pitch
(15) flap, possibly the [ ] possibly
(16) some of the regions of the fixed trailing
(17) edge.
(18) Q. And is it consistent with your
(19) recollection that that was in the same line of
(20) materials that Rockwell was using on the Space
(21) Shuttle, that Lockheed provided to Rockwell?
(22) A. It was my impression that the
(23) materials were derived from those same kind of
(24) materials. They may not have been identical,
(25) but it was that line of technology that

Page 172
developed that kind of material.
Q. Do you recall that Rockwell used reasonably small pieces of tile in, for example, a mosaic formation, and you were looking for much larger pieces?
A. We were looking for larger pieces and shaped pieces, although ours did not necessarily have to be very large. We could have put strain isolation layers and so forth on it. But it was certainly not identical probably to the Space Shuttle tiles.
Q. Do you recall having discussions with Lockheed later about materials other than that thermal tile?
A. I don't recall any. There may very well have been some, but I would not have been involved in those discussions personally.
Q. Is it your recollection that you expected that you may have gotten more useful information from the B-2 program?
A. Yes.
Q. Is it your recollection that the B-2 technology was also older than the A-12 technology?

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A. In some respects it was, in some respects it wasn't. The A-12 I think had

better signatures in general than the B-2 had. There were different approaches taken in different places, and the B-2 was a much larger airplane. A lot of the B-2 information that would have been most valuable to the A-12 was not signature information, however.

Q. Do you recall at some point in 1990 indicating in an interview or a meeting that – and when I say you, I'm meaning you, Dr. Jackson – saying that, after reviewing the B-2 data, you concluded that there was not much that you would have done differently, that the B-2 used fairly old technology, and that the technology would not have changed much of what you did on the A-12?

A. I don't specifically remember saying that, although that probably would have reflected my opinion.

Q. So that's consistent with your recollection?

Yes.

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Q. And do you also recall – or do you recall having said also in 1990, either in an interview or in a meeting, that with regard to schedule and weight, if you had had a better idea of what the B-2 went through, you would have planned better, but that your technology

was better and in fact you beat out the B-2 team for the A-12 contract?
A. I think that's probably also fairly accurate.
Q. So that's consistent with your recollection?
A. Yes.
MR. SCHOONER: Can we go off the record for one moment.
(Discussion off the record.)
(Jackson Exhibit No. X-74 was marked for identification.)
BY MR. SCHOONER:
Q. The Court Reporter is handing you what he's marked as Exhibit 74. Do you recall ever having seen this document before?
A. I don't recall having seen this particular one before.

you were
(15) read into the B-2 program in September or October 1988. Is
(16) that correct?
(17) A. Yes.
(18) Q. Okay. Was there someone from the Navy who
(19) facilitated your being read into the B-2 program?
(20) A. As I recall, Jeff Cook spearheaded the effort
(21) to get the initial contacts made with the Air Force.
(22) Q. Okay. Do you recall in that timeframe that
(23) you were read in any discussions between yourself, Jeff
(24) Cook, and Dr. Jackson, Keith Jackson, regarding the means by
(25) which information would be exchanged between the A-12

Page 114
(1) program, GD/McAir, and the B-2 program?
(2) A. Yes.
(3) Q. What do you recall about those conversations?
(4) A. We held conversations between General
(5) Dynamics and McAir regarding the advisability of directed
(6) discussions with Northrop Corporation. It

was my
recommendation that we not meet directly with Northrop
because of the possibility of proprietary rights infringement, that is Northrop propriety rights
infringement.
It was my suggestion that –
Q. Could I just stop you there, please? When you say possibility of proprietary rights infringement,
Northrop proprietary rights infringement, are you saying
that you were concerned that proprietary rights held by
Northrop could be infringed?
A. That's right.
Q. Okay. Please go ahead then.
A. That we could inadvertently perhaps utilize
information that Northrop considered proprietary and
subsequently get involved in a lawsuit. I had been involved
in the lawsuit between McDonnell Douglas and Northrop on the
F-18 and had spent quite a bit of time working on that
particular lawsuit and was very sensitive to the possibility
of getting into inadvertent litigation as a result of

inadvertent proprietary information usage.
Q. Okay. In this area, I want to be clear up front, and I will caution you with or before your counsel does. I am not asking for privileged communications between you and counsel, okay, and I do not mean to, and I want to make sure my question does not elicit that, okay?
A. (Witness nodded indicating an affirmative response.)
Q. But, please, if you could explain for me what you meant when you said that you had spent quite a bit of time working on that lawsuit between McDonnell Douglas and Northrop? How did you spend quite a bit of time working on that lawsuit?
A. I participated in the document research for the lawsuit. I participated in some of the write-ups that were done that were utilized for the lawsuit.
Q. Were these factual write-ups?
A. I don't recall now.
Q. Okay.
A. And I was deposed twice as part of that lawsuit.
Q. Okay. What was the outcome of that lawsuit?
A. The lawsuit was finally settled. I don't

remember the date, but it was finally settled between
Northrop and McDonnell Douglas out of court.
Page 116
Okay. You stated that there were
conversations held between McDonnell Douglas and General
Dynamics regarding the advisability of direct communications
with Northrop. Do you recall stating that?
A. Yes.
Q. Who participated in those discussions between
McDonnell Douglas and General Dynamics?
A. Myself, Harry Snodgrass, John Lamers, Keith
Jackson. Those are the names that I can recall.
Q. Can you recall anyone else being present in
these discussions who you just cannot remember their –
A. There may have been others that I don't
recall.
Q. Of the three other gentlemen you mentioned,
do you recall any others who shared your concern regarding
inadvertent litigation?
A. Yes. Mr. Snodgrass was also concerned about
the potential for litigation.
Q. Okay. Do you recall whether Dr. Jackson

favored direct communications with Northrop or instead using the Navy and Air Force as conduits of the information?

A. I don't recall that Keith had a position. He may have; I just don't recall.

Q. Do you recall if Captain Cook had a preference as to how the information would be exchanged

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between the contractors on the A-12 and Northrop?

A. I don't recall that he had a preference.

Q. Okay. You mentioned that there were discussions between yourself, Mr. Snodgrass, Mr. Lamers, and Dr. Jackson. Do you recall how many discussions you had on this issue?

A. No.

Q. Okay.

A. More than one.

Q. Okay. At any of those discussions, do you recall counsel for either McDonnell Douglas or GD being present?

A. I just can't recall who was – who else was involved.

Q. Okay. On the F-18 program, do you recall if there was a proprietary agreement between Northrop and McDonnell Douglas?

A. I don't recall.
Q. Had you ever been involved in any other programs that caused you concern regarding the inadvertent disclosure of proprietary data other than the F-18?
A. I had been involved in other programs that required use of proprietary data, yes.
Q. Did a problem arise regarding the inadvertent release of proprietary information?

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A. On the other program?
Q. Yes.
A. No.
Q. (Farr Deposition No. 120 was marked for identification.)
BY MR. KIRSCHMAN:
Q. Mr. Farr, I am going to ask you to please review what the court reporter has marked as Deposition Exhibit No. 120.
A. I've reviewed the document.
Q. Okay. Do you recall, Mr. Farr, seeing this document, the draft agreement and the cover slip, any time prior to today?
A. No.
Q. In this timeframe, August 15th of 1988, were you aware of the existence of a draft proprietary data agreement?

A. No.
Q. Looking at the first page of the exhibit, page 144, do you know who Pat Hogan is?
A. Yes.

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Q. (U) The difference in then year . . . dollars between the two proposals was approximately $7.8 billion; correct?

A. (U) For FSED.

Q. (U) For FSED.

A. (U) For 1, 2, and 3.

Q. (U) Right.

A. (U) Given, of course, they didn't propose Lot 3.

Q. (U) Right.

A. (U) Yes.

Q. (U) Did that fact concern you when you were doing your estimate?

A. (U) No. Let me explain why. If you looked at the details of the Northrop proposal, and let's just take the three big areas that make up FSED for a second: the design engineer hours, the test and evaluation, and the manufacturing.

(U) The McDonnell Douglas/GD estimate was very significantly higher than the Northrop estimate in each of these areas. You go back 22 percent higher for the design engineering

hours and the test and evaluation. The manufacturing was about 10 percent higher in the McDonnell Douglas/GD estimate.

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(U) What I'm really saying here is Northrop did nothing in the estimating to lead you to believe that they thought the plane was going to be harder to build or more expensive than McDonnell Douglas/GD. In fact, just the opposite was true. A lot of the difference in full scale development is made up by two things: The 580 million we talked about earlier, plus a difference in inflation rates that amounts to about 6 percent. If you take that out, or if you compare the prices of the two airplanes, they're actually very close.

(U) Now, there is another large difference in the numbers in the production lots. None of this is in the actual calculation of the cost or price of the plane. All of this is driven by a ceiling factor, a price to ceiling factor of about 75 percent that, Northrop added at the end.

(U) So what I'm really telling you

is that Northrop showed us nothing in a proposal to allow us to believe that based on any B-2 or other experience that this plane would cost more than what GD/McAir thought. All Northrop did was add on a very high factor at the end of everything. (U) And the general feeling since they did it this way, as opposed to showing us

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anything in the estimate that would lead you to believe that it was higher, our general feeling was that they simply thought they had the program won and were trying to make as much profit as they possibly could get on it. And in fact, we increased the Northrop estimate in certain areas where we lowered the McAir/GD estimate.

Q. (U) Do you recall what areas those were?

A. (U) The design engineering hours section, the system test and evaluation section.

(U) Now, had they done anything in any of the estimating areas, showed us that it should have been a lot higher we could have been

very concerned. Had they used a rationale in any of these factors that they added – this 75 percent factor that they added at the end that indicated this was because of their concern, then we, again, would have been concerned. (U) This was simply something that they stuck in there. So, yes, we looked very close to see if there was a problem because of it. But that was not the way they had done it. Q. (U) Didn't the fact that they had basically submitted a technical proposal that was

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unresponsive and bid less aircraft for more money generate that sort of concern with the cost group? A. (U) It generated more of a concern that they weren't taking things seriously and that it looked like they were trying to almost rip off the government more so than anything else. (U) Had they legitimately presented anything that backed this up, then it would have been a totally different concern on the

government's part.
(U) And I think what you have to remember on top of this is that what we were estimating was significantly higher than anything in our database, even a supersonic swing wing F-14. We were well higher than that by 28 percent manufacturing; by 25 percent design engineering hours. So we were doing our best to cover this and had we seen – by cover this, I mean cover this new technology, and had Northrop showed us anything that was definitive or specific, we would certainly have jumped at that, but they did not.
Q. (U) Do you know whether or not Northrop was asked to show you something definitive after the review of their initial proposal?
A. (U) I think they were, but I was

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not there. Nothing came down. I know all the aspects of it were questioned and nothing came down through the people that had been there, to me, that Northrop responded in any way as to why these things should be that way. And believe me,

we were
certainly looking for anything like that because
this was new technology.
Q. (U) The historical database that you used to do this estimating work, did that database contain only Navy aircraft?
A. (U) No. The F-15 I already mentioned and the F-16 are Air Force aircraft.
Q. (U) Do you recall that there was a $4.2 billion cap on the FSED program at this time?
A. (U) No one ever mentioned anything to me about a cap. If there was one I was never
aware of it as such. And we did not estimate toward anything – you know, toward any kind of a
cap. We estimated it as we understood it.
(U) I think one other comment on the Northrop thing is our estimate and Northrop's, apart from these couple of factors, were quite close.
Q. (U) Does that show up in any of your charts in the cost presentation to the SSAC?

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Aside from the fact that the estimates were quite
close. For example –
A. (U) It doesn't for the production lots because we didn't put the detail in here.

Q. (U) Just for the FSD?
A. (U) For the FSED. And that's another point to be raised. They did not have that very high 75 percent factor in FSED, so if this was a real problem, why not put it in. But if you compare our FSED you will see that we are fairly close to Northrop in our estimate.
Q. (U) You said this 75 percent factor, are you talking about the share ratio?
A. (U) No. On top of the price and the production lots, they had a factor to go to ceiling of around 75 percent and that's what made those numbers so high and contributed to that $7 billion difference you pointed out.
Q. (U) Is it a fair interpretation that Northrop added that because of risks they perceived in the FSD part of the program?
A. (U) They certainly didn't state it that way.
Q. (U) How was it stated?
A. (U) They really didn't state

Page 73
Q. So assuming the date is correct, it would have been in July of '90?
A. That was really the only time I got interviewed.
MR. GRAHAM: Mr. Magnus, just one note.
MS. OHTA: Excuse me, Counsel.
MR. GRAHAM: Counsel, if I may finish.
MS. OHTA: Are you making an objection on the record?
MR. GRAHAM: I'm going to instruct the witness with regard to an issue of privilege.
MS. OHTA: You're going to instruct him not to answer a question based on privilege? There's no question pending.
MR. GRAHAM: Counsel, may I finish?
MS. OHTA: I just think it's inappropriate for you to be giving Instructions.
MR. GRAHAM: Counsel, may I finish?
MS. OHTA: No question is pending.
MR. GRAHAM: I haven't said a word about what it is. You don't even know what
Page 74
I'm going to say. May I finish?
MS. OHTA: Please.

MR. GRAHAM: Thank you. Mr. Magnus, I understand you have testified that you only recall one meeting, and based upon the notes you believe that to be this meeting. I'm going to instruct you that to the extent you believe you had another meeting other than the ones referenced in this document, Exhibit number 22, that that is potentially privileged, and if you believe there was another conversation at another time you and I need to have a conversation about that.

(You) MS. OHTA: That's fine. But I just think you're coaching him. I think Mr. Magnus testified that, to the best of his recollection, there was only one occasion when he met with an attorney to discuss the A-12 program.

BY MS. OHTA:

Q. And it may have been one or two days, but it was one occasion as opposed to two separate interviews separated in time; is that fair?

A. That's is what I recall.

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MR. GRAHAM: And I'm not taking issue with that, Counsel. Just the fact is that Mr. Magnus has also testified that he thought that there was an interview that occurred after termination. If such an interview occurred, if he recalls events from that, which he has not at the moment, but that is potentially privileged and he needs to stop and we need to talk about that.

That's all I'm saying.
MS. OHTA: That's fine, Counsel, but I didn't ask him about any meeting or the contents of any meeting he had with an attorney after termination.
MR. GRAHAM: I appreciate that, and I'm merely instructing the witness.
MS. OHTA: I recognize that is potentially privileged.
MR. GRAHAM: I am not having a problem with your questions. I'm instructing the witness that he may discuss the meetings referenced in document number 22, but any other meetings with counsel, if he remembers them, he should not discuss those until we have had an opportunity to talk about them.

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That's all I'm saying.
BY MS. OHTA:
Q. Just to clarify, it is your recollection, based on reading the notes of this apparently two-day interview with a Mr. Eastburn, that, to the best of your recollection, this is the only time that you had an discussion with any GD attorneys concerning the A-12 program other than perhaps a discussion within the last couple of days with the attorneys present here?
A. I recall having an interview with a GD attorney at one time towards the end of the program. My recollection was that it was after termination, and so I guess now – so there is notes here saying this was an

interview. So I'm sure I had this one. I don't know if there was another one. I mean, I thought there was just one.
Q. And you testified that, to the best of your recollection, this is an accurate representation of what you said at the time?
A. Sure.
Q. So as of July of '90, July of '90 would have been a relatively short time after

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the technology transfer with B-2, the meetings we discussed yesterday, the meeting or meetings?
A. Do you remember the dates on those documents? I just don't remember the exact date. I mean, we could look at the dates and figure it out.
Q. So is it fair to say that in July of '90 it was your opinion that you weren't sure that the technology design of the B-2 would have impacted on the A-12?
A. I think it is fair to say that what we found out was that they didn't have a lot to offer us. However, it would have been nice to know that earlier.
Q. If you want to follow along, it's page 1208.
A. Okay.
Q. According to these notes, Mr. Eastburn was apparently recording what you were telling him, and he recorded that you were not sure technology design on B-2 would have

impacted
(23) on the A/C, meaning the A-12.
(24) A. That is correct.
(25) Q. And you still believe that that was
Page 78
(1) accurate at the time?
(2) A. I still believe that.
(3) Q. And you still believe that?
(4) A. Yes.
(5) Q. And on page 1211 is the statement
(6) accurate that in your opinion as a result of
(7) this B-2 technology transfer you learned that
(8) you were not really doing anything really
(9) wrong?
(10) A. That's correct.
(11) Q. And in your opinion, based upon this
(12) B-2 technology transfer, there were no
(13) revelations made by B-2 SPO or the Northrop
(14) people?
(15) A. That's correct.
(16) Q. And that it was your opinion in July
(17) of 1990, looking at page 1212, it was your
(18) opinion in July of 1990 that if this B-2
(19) technology transfer had occurred before GD
(20) bid on the A-12 contract the impact might
(21) have been that you would have confirmed
your
(22) estimations of what was hard and what was
not
(23) hard, but the bid would not have been
(24) changed?
(25) A. That is my opinion, based on saying

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we were in the throes of competition. I believe that's what it says here. And of course I really wasn't in a position to make a bearing on that answer, but that was just my opinion, yes.
A. And what was your opinion based on? At the time I guess I can't think of what it was based on, but I just believe, hey, we were in the throes of a competition, and we were trying to win this thing. So you're going to bid it as tightly as possible.
Q. Who is Wayne McGregor and what role did he play on A-12?
A. Wayne McGregor at that time was the manager of observables technology, and he really didn't work directly on the A-12 program. He was kind of our overall functional manager. So he took care of kind of the other side of the house that wasn't on the specific program.
Q. On page 1214, there's a note concerning MFA.
A. Yes.
Q. Was it your opinion in July of 1990
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that the technology for the MFA both in terms of the antenna and in terms of RCS was pushing the limits of technology?
A. Yes. You bet.
Q. And would that have been your opinion in January of '88, at the time of contract

formation?
A. At that time, I would have probably said I wasn't sure, because I hadn't spent a lot of time working on the antennas. But during the program, during the FSD part, I started working some with the avionics people to try to bring those things around, try and make them meet the requirements.
Q. Was it your opinion in July of '90 that it was unachievable or simply that it was pushing the limits of the technology?
A. I know I thought it was pushing the limits of technology. I don't have any basis to recall whether or not I thought it was unachievable. The day of the program termination, I had traveled out to Gray Butte with an MFA to run some tests to try to validate a design. We never got to run those tests.

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So I don't know where we would have finally ended up, because we came up with some unique design concepts to try to balance the gain and the RCS.
Q. When were those designs developed in relation to this July '90 time?
A. They were developed throughout the program on the MFA. I have a hard time sticking dates on things, because to me it's kind of a long blur of work. But they matured as we went along.
We evaluated all kinds of different options on the MFA to make sure we got the

RCS out of it, and tried to maintain the gain.
Q. Well, if the testing was January of '91, when you were going out to Gray Butte –
A. Right.
Q. – do you have any idea how long it had been since the last prior test of the MFA had been done?
A. No, I don't. But I'm sure we can look back at program records and reconstruct that.
Q. So is it reasonable to assume that

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these unique design changes that you are referring to would have been made in the latter part of '90, if you were going out to do the testing in early '91?
MR. GRAHAM: Objection, calls for speculation.
THE WITNESS: We would have likely –
MS. OHTA: The question was not for him to speculate. The question was was it reasonable to assume.
MR. GRAHAM: The witness has said he doesn't know the answer, and you're asking him, in my opinion, to guess, reasonably or otherwise.
THE WITNESS: I think it is reasonable to assume we were building parts in late 1990. As far as when the design firmed up to build those parts, I know that the design we were looking at was a unique way of building a |

(21)
(22)
(23)
(24)].
(25) And there was some development work
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(1) along the way by the avionics folks to come
(2) up with that. I just don't remember all the
(3) time sequencing of when it all happened.
(4) BY MS. OHTA:
(5) Q. In your opinion, was it late in the
(6) program to be doing those kinds of design
(7) changes to the MFA?
(8) A. At this time, I thought that those
(9) were things we can get into designs to get it
(10) on the airplane. I don't believe that there
(11) are hard, fast rules that say, all right, at
(12) this point of the program you have got to
(13) have every single one of these items closed
(14) and at this point you've got to have every
(15) single one of these.
(16) There's always, on any kind of an
(17) aircraft development program that's
something
(18) new, there are always going to be things that
(19) stick out that are pushing technology, and
(20) you're going to have to extend work on some
(21) of those things.
(22) So I think things like that are
(23) expected. Would it have been nice to have
(24) had a design in hand before then? Sure.
(25) Q. Were you involved in making schedules

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and establishing milestones on the A-12 program?

A. I was involved with setting up some of the tests and that sort of thing, but not overall milestones about, you know, when the aircraft have to be built and stuff like that, no, not that kind of milestone.

Q. But you were familiar with schedules as to when certain things were supposed to be accomplished?

A. Kind of at a high level, yeah, at a real high level. But I know that there were things that we didn't have designs finished, but we had to keep going when there are certain issues that don't get closed out. And that's normal for a program like this.

Q. Was it important or did management convey to you that it was important or not important to stick to the schedules that had been established?

A. I believe it's conveyed that sticking to the schedules are important, but at the same time another message that's conveyed by both management and the customer is, we want to try to meet all the requirements. So if

(21) MR. LIGUORI: Dr. Jackson, you've got to
(22) let him finish the question or the court reporter

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(1) can't get it down.
(2) THE WITNESS: Excuse me. It would add
(3) weight and flow losses and complexity to the
(4) airplane, and so if it were not needed, we certainly
(5) didn't want to put it in.
(6) BY MR. KIRSCHMAN:
(7) Q. ( ) Under the propulsion system
(8) configuration, it is also noted the engine, the
(9) F404/F4D1 and under that the "new multi-louvered
(10) ejector nozzle, high AR nozzle opening." Do you see
(11) that?
(12) A. ( ) Yes.
(13) Q. ( ) Do you recall why at this time –
(14) and you specifically – at this time on June 5, the
(15) day of the configuration review, there was a
(16) decision made to go with the MULE?
(17) A. ( ) I think that after we got the inputs
(18) from all the propulsion community, that we felt that
(19) there was enough potential that this would work and
(20) meet the Navy's needs that we needed to go

work the
(21) design aggressively. And the way you do that is to
(22) make it your baseline so you focus on it and work on
Page 488
(1) it hard. If you don't make it a baseline, you don't
(2) work on it hard.
(3) So we felt that we had enough information
(4) on it at that time that it was worthwhile giving it
(5) a major effort.
(6) Q. ( ) Do you recall if there were any test
(7) results that you reviewed on June 5 that supported
(8) that decision?
(9) A. ( ) I do not remember any.
(10) Q. ( ) Did you believe, as of June 5, 1986,
(11) that the use of the MULE would give you a
(12) competitive advantage over your competition?
(13) A. ( ) Our feeling was that it was
(14) something that gave us a good chance of meeting the
(15) Navy's needs. We didn't know what the competition
(16) had, so it was hard to say how we fared vis-à-vis
(17) the competition.
(18) (Jackson Exhibit 137 identified.)
(19) BY MR. KIRSCHMAN:
(20) Q. ( ) Dr. Jackson, Exhibit 137 is a
(21) two-page document. The second page of the

document
(22) is a briefing chart from General Dynamics, and it is
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(1) encaptioned "review of competitive situation." The
(2) front page of the exhibit indicates that it existed
(3) at least as of April 10, 1986, because it is signed
(4) for by Mr. Lamers and Mr. Snodgrass.
(5) MR. LIGUORI: Where do you see the date,
(6) Bob?
(7) MR. KIRSCHMAN: You will see where the
(8) requesters are indicated, and apparently they
(9) requested it from security on April 10, 1986.
(10) MR. LIGUORI: Okay.
(11) MR. KIRSCHMAN: Both on the same day.
(12) MR. LIGUORI: Thank you.
(13) MR. KIRSCHMAN: Let me know when you've
(14) had a chance to look through that document.
(15) (Witness reviewed the document.)
(16) THE WITNESS: Okay.
(17) BY MR. KIRSCHMAN:
(18) Q. ( ) Have you seen this Vugraph before?
(19) A. ( ) I don't remember it today. I'm sure
(20) I have, however.
(21) Q. ( ) Why are you sure you have?
(22) A. ( ) Because I would tend to look at
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(1) these things that the bosses on the program put out.

Q. ( ) In this time frame, GD had a relatively small group involved in the ATA?
A. ( ) Yes, relatively small.
Q. ( ) The Vugraph has a caption that states "review of competitive situation."
A. ( ) Right.
Q. ( ) And the first bullet there says "east-went team has two major, nontechnical advantages." First is "Grumman business base as Navy contractor," and the second is "California, New York, Texas political base."
Do you see that?
A. ( ) Yes.
Q. ( ) The second bullet states "and Northrop has a technical advantage in stealth because of ATB and other experience." Do you see that?
A. ( ) Right.
Q. ( ) First, do you know who prepared this briefing slide?
A. ( ) I presume it was Lamers and/or

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Snodgrass.
Q. ( ) You did not?
A. ( ) No.
Q. ( ) As of April 10, 1986, did you believe that Northrop had a technical advantage in stealth because of the ATB?
A. ( ) I did not know what Northrop's

technical status was on the airplane. I did know
that –
Q. ( ) On the ATB?
A. ( ) On the ATB or on the ATA, or on the
A-12. I did know that Northrop had worked on the
ATB or the B-2, and the rumors we had heard was
there was a lot of money going into it.
Q. ( ) And you knew that as of April 1986?
A. ( ) Right. And so I think it was a good
assumption that they would have an advantage because
of that, because of the resources going into that
program.
Q. ( ) Did you have an understanding in
April of 1986 that the ATB was involved with stealth
technology?

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A. ( ) Yes, that was public knowledge at
that time.
Q. ( ) That was public knowledge?
A. ( ) Yes, it was.
Q. ( ) In April of 1986?
A. ( ) Yes, it was.
Q. ( ) I believe in looking at the last
exhibit related to the configuration selection, when
I asked you whether there was a competitive
advantage to your selecting the MULE in the

baseline
configuration, you stated that you couldn't answer
that because you weren't aware of anything related
to your competitors' situation?
A. ( ) Yes.
Q. ( ) Is that – I don't mean to misstate
your testimony.
A. ( ) No, that's still correct.
Q. ( ) That's still correct?
A. ( ) Sure.
Q. ( ) But you knew generally that the ATB
was involved in developing stealth technology?
A. ( ) Right.

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Q. ( ) Do you consider the use of a nozzle
to be a component of stealth technology on the A-12?
Q. ( ) Sure. Of course, I had no idea what
sort of nozzle they had.
Q. ( ) Did you ever ask the Navy to tell
you what type of nozzle Northrop was using on the
ATB?
A. ( ) No.
MR. LIGUORI: At what time?
BY MR. KIRSCHMAN:
Q. ( ) On or about June 1986?
A. ( ) No, we didn't ask them what kind of
a nozzle they had. We asked them for information

(14) that they thought would be useful to us on the
(15) program. We didn't know what to ask for on the ATB.
(16) Q. ( ) Well, you knew the ATB had a nozzle;
(17) right?
(18) A. ( ) Sure.
(19) Q. ( ) Did you think it would be useful to
(20) know what nozzle the ATB was incorporating in their
(21) design?
(22) A. ( ) Sure.

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(1) Q. ( ) Then why didn't you ask the Navy for
(2) that information in approximately June 1986?
(3) A. ( ) We asked them broadly for any
(4) information from the ATB that would be useful to us,
(5) in stealth or other areas, from the ATB program.
(6) Q. ( ) In June 1986?
(7) A. ( ) I can't remember the time period.
(8) Both I and Pike Farr in particular talked to the
(9) Navy people on quite a few occasions and requested
(10) information from the ATB program to help our
(11) efforts.
(12) Q. ( ) I can appreciate you can't recall
(13) exact time frames. Do you recall during concept
(14) formulation, asking the Navy to tell you what nozzle

was being incorporated in the ATB design?
A. ( ) I can't specifically remember whether we asked about specifically a nozzle or not.
We may have. I just don't remember.
Q. ( ) During concept formulation?
A. ( ) During concept formulation, yes.
Q. ( ) But getting back to the document regarding the baseline configuration selection, it

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is your testimony that selection of the MULE had
nothing to do with giving GD and McAir a competitive
advantage in the selection process?
A. ( ) Any decision that you make on an airplane when you're in a competitive situation has
an impact on the competitive process. It was not
specifically driven by a knowledge of, in any way,
what the competition was doing. It was driven by
the Navy's passing on information to us, and me in
particular, that our nozzle design previously wasn't
good enough.
And so if our nozzle wasn't good enough,
you could say yes, that impacted the competitive

situation, if Northrop's nozzle had been good enough. I didn't know that either. I didn't know whether they were giving us both the same information. I simply was in the dark about that.

Q. ( ) Now, let's just talk specifically about the nozzle for now.

A. ( ) Sure.

Q. ( ) You said any information that you could get from the ATB regarding the nozzle would be

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helpful.

A. ( ) Sure.

Q. ( ) I believe that's how you put it?

A. ( ) Yes.

Q. ( ) Did you believe you could not proceed in the designing of the MULE without information from the ATB related to their nozzle?

A. ( ) Oh, obviously not.

Q. ( ) Did there ever come a point during the FSD program where you determined that you absolutely needed information from the ATB in order to incorporate the MULE into the A-12 aircraft?

A. ( ) No.

Q. ( ) Could you turn to the last page of Deposition Exhibit X136. Again, that's a document

talking about the baseline configuration selection.
Do you see on this last page of the exhibit, it lists a configuration evaluation plan?
A. ( ) Yes.
Q. ( ) And it gives dates?
A. ( ) Right.

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

PLAINTIFFS' RESPONSES TO DEFENDANT'S FIRST SET OF CONTENTION INTERROGATORIES

Pursuant to the Court's order dated August 11, 2000, the contractors provide the following responses to Defendant's First Set of Contention Interrogatories. As recognized by the Court, our contentions and these responses are continuing in nature and will be modified as appropriate during the course of discovery in this case.

* * * *

Contention Interrogatory No. 6:

Do you contend that any individual requirement, task, or technical specification of the FSED contract was impossible at the time of contract award? If so, identify each such requirement, task, or specification and, separately for each:

(a) State whether you contend that it was impossible to perform as being beyond the state of the art.

(b) State whether you contend that it impossible to perform upon grounds of commercial impracticability.

(c) Explain why it was impossible to achieve.

(d) Identify when you determined that it was impossible to achieve.

(e) Identify all individuals who determined that it was impossible to achieve.

(f) Identify each fact witness you expect to call to testify at trial in support of your contentions in your response to this interrogatory.

(g) Identify each expert witness you expect to call to testify at trial in support of your contentions in your response to this interrogatory, and for each expert witness:

(i) Identify each opinion you expect the expert to render in his or her testimony.

(ii) Identify each basis for each opinion you expect the expert to render.

(iii) Provide any draft and final reports prepared by the expert.

(iv) Produce all workpapers produced by the expert and any documents provided to or considered by the expert in forming his or her opinions.

(h) Identify each document you expect to use at trial in support of your contentions in response to this interrogatory.

Response:

No. The contractors do not contend that any individual requirement taken in isolation was impossible. The contractors' contentions regarding impossibility and commercial impracticability are set forth in response to Contention Interrogatories Nos. 7 and 12.

Contention Interrogatory No. 7:

Do you contend that any of the contract requirements, tasks, or technical specifications of the FSED contract, if not individually impossible, were impossible to achieve in combination with other

contract requirements, tasks, or technical specifications? If so, identify each such combination of contract requirements or technical specifications and, separately for each:

(a) Explain why the combination of contract requirements or technical specifications was impossible to achieve.

(b) Identify when you determined that the combination of contract requirements or technical specifications was impossible to achieve.

(c) Identify all individuals who determined that the combination of contract requirements or technical specifications was impossible to achieve.

(d) Identify each fact witness you expect to call to testify at trial in support of your contentions in your response to this interrogatory.

(e) Identify each expert witness you expect to call to testify at trial in support of your contentions in your response to this interrogatory, and for each expert witness:

(i) Identify each opinion you expect the expert to render in his or her testimony.

(ii) Identify each basis for each opinion you expect the expert to render.

(iii) Provide any draft and final reports prepared by the expert.

(iv) Produce all workpapers produced by the expert and any documents provided to or considered by the expert in forming his or her opinions.

(f) Identify each document you expect to use at trial in support of your contentions in response to this interrogatory.

Response:

The contractors cannot respond fully to this interrogatory because discovery in this area has been suspended during most of the pendency of this litigation. Based on currently available information, the contractors state as follows:

The Court already has found that the Navy knew that the weight specification was "unachievable." (35 Fed. Cl. at 373.)

The contractors also contend that the weight, price and schedule terms of the contract, in combination with each other and in combination with the performance and low observability specifications, were impossible and commercially impracticable. As the government knew before award, the sum total of the requirements of this contract was impossible.

(a) The cost, schedule, weight, performance and low observability aspects of the A-12 contract were highly interrelated. Whereas certain

specifications and performance levels could be met in isolation, integrating an aircraft that met all of the specifications, within the weight specification and within the cost and schedule of the FSED contract was impossible and commercially impracticable.

The radar cross section specifications that drove the aircraft design to a flying wing configuration could not be met on a specification compliant, BAFO weight aircraft. The Navy has acknowledged as much. It determined before award that it could not get everything it wanted out of the A-12 and still meet all of the weight-related requirements. For example, NAVAIR Commander Wilkinson specifically advised Vice Admiral Dunn before contract award that certain weight related requirements would not be met. Dr. Somoroff, the Navy official who signed the contract specifications, thought that as a matter of conscience, Admiral Dunn should be informed that the weight specification, and certain weight related requirements, would not be met.

During performance and even after termination, the government confirmed that the weight-related requirements could not be met in combination with the totality of the A-12 specifications. Among other things, in September 1989, the Navy's chief engineer concluded that the specification weight was not achievable. Further, after termination, the Navy's engineers wrote close-out memoranda stating that the Navy's projected IOC weight for the plane as designed -- which was 7930 pounds more than the

contract weight -- was near minimum weight for the then-existing requirements.

The contract price and schedule requirements were impossible to achieve and commercially impracticable because of the difficulty and expense entailed in developing a carrier suitable, very low observable flying wing aircraft -- challenges far greater than the contractors knew or could have known when they agreed to the contract terms. The Navy had been informed by Northrop, who had built the only low observable flying wing production aircraft in existence (of which the contractors are aware), that the price, schedule, weight, and other contract specifications could not be achieved. An aircraft meeting all of the FSED contract specifications was impossible and commercially impracticable to develop at the contract price and on the contract schedule. Indeed, the government admitted as much when it extended the original schedule by 18 months without any additional consideration.

(b) The contractors determined during contract performance that the combination of contract requirements and technical specifications was impossible to achieve.

(c) Among others, the Court, Dudley Cate, Rear Admiral Jeffrey Cook, Admiral Dunn, Pike Farr, Keith Jackson, John Lehman, Margaret Olsen, Russell Perkins, Dr. Somoroff, and Admiral Wilkinson. The contractors expect to identify additional persons with knowledge as they resume

discovery in this area where discovery was previously suspended.

(d) The contractors have not yet made a final selection of the fact witness they intend to call regarding these issues. We believe that the list of potential witnesses with knowledge about these issues includes those individuals listed in response 7(c) above.

(e) At present, the contractors are considering whether to call expert witnesses regarding these issues. If the contractors decide to call any such experts, they will notify the government in a timely manner.

(f) At present, the documents the contractors intend to rely upon include the following:

1. (3/1/87) Northrop Proposal, Technical Reports, Report 5, Weight and Balance (212//008632/87).

2. (3/1/87) Northrop Proposal, Business Executive Summary (212//010899/87).

3. (1987) Northrop Proposal, BAFO Revision, Technical Report 31, Deviation Impact, Level 4 (212//021727//87).

4. (8/5/86) Northrop/Grumman/Vought ATA Team Draft ATA Acquisition Strategy Review/Comments (206//00234-93).

5. (4/21/87) Minutes of the SSAC (Ex. 4023).

6. (7/86) Bravery Executive Review (LIT//1985-93).

7. (3/11/91) J.A. Cook, A-12 Lessons Learned Presentation (206//01 77-93).

8. (4/25/91) A-12 WTB Memorandum of Record (Ex. 5673).

9. A-12 Weight Status, Capt. Jeff Cook (Ex. 6).

10. (9/15/87) Northrop Proposal, Executive Summary, BAFO Revision (212//020172/87).

11. (2/14/91) Memorandum from AIR-5117 E to PMA-235C re: Congressional Testimony/ Answers For OP-05.

12. (3/02/90) SPRG Review of the Bravery Program (Ex. 1046).

Contention Interrogatory No. 9:

Do you contend that the Navy failed to disclose to the contractors any vital information that affected the performance, cost, or duration of the FSED contract? If so,

(a) Identify each such piece of vital information, the relevant contract requirement or technical specification to which the information

related, and explain why the information was vital to the contractors' performance.

(b) State whether you contend that the Navy did not offer in 1988 to arrange direct communications between the Northrop B-2 contract organization and the contractors' A-12 organization to facilitate the exchange of technical or other information, and that the contractors did not refuse, in 1988, to participate in such a direct contractor-to-contractor exchange, and the full factual basis for your contention.

(c) Identify each fact witness you expect to call to testify at trial in support of your contentions in your response to this interrogatory.

(d) Identify each expert witness you expect to call to testify at trial in support of your contentions in your response to this interrogatory, and for each expert witness:

(i) Identify each opinion you expect the expert to render in his or her testimony.

(ii) Identify each basis for each opinion you expect the expert to render.

(iii) Provide any draft and final reports prepared by the expert.

(iv) Produce all workpapers produced by the expert and any documents

provided to or considered by the expert in forming his or her opinions.

(e) Identify each document you expect to use at trial in support of your contentions in response to this interrogatory.

Response:

Yes. The contractors cannot respond fully to this interrogatory because discovery in this area has been suspended during most of the pendency of this litigation. Based on currently available information, the contractors state as follows:

(a) Before contract award, the government possessed, but failed to disclose, vital information from other classified programs, including the B-2 program, that was essential to bidding on the A-12 contract. In particular, this information was essential to predicting the time needed to develop an aircraft that would meet the Navy's requirements, the weight of such an aircraft, and the amount of money it would cost. The government was obligated to divulge this information to the contractors, to give the contractors an adequate warning regarding this information or to otherwise protect the contractors from their lack of information, such as by structuring the contract differently.

The government possessed superior knowledge from other classified programs, including the B-2 program, that the cost to develop and produce a very

low observable flying-wing aircraft greatly exceeded, and could not be accurately predicted from experience with, conventional aircraft. Among other things, the government knew that an aircraft such as the A-12 would cost at least 8-17% more to develop than conventional aircraft, with the percentage increasing as the size decreases. A carrier based aircraft, which is necessarily smaller than some land based aircraft (such as the B-2), therefore would suffer huge cost penalties. Indeed, Northrop specifically informed the Navy of these facts in its response to the Navy's acquisition strategy. The Northrop ATA bid highlights the government's superior knowledge with respect to the true cost to produce the A-12. The Northrop bid, which was based on Northrop's vast B-2 knowledge, was $1.14 billion more than the McDonnell Douglas/General Dynamics bid for the FSED contract alone. The cost differential was even greater on the FSED and Lots I, II, and III options, a $7.72 billion spread. Not only was Northrop's bid much higher, but Northrop bid two fewer FSED planes, refused to bid on a fixed price basis, and capped its own liability on the contract at $400 million. While Northrop possessed some of the government's superior knowledge, the McDonnell Douglas/General Dynamics team did not.

The government recognized before award that McDonnell Douglas and General Dynamics did not have the information that they needed to submit an informed bid on the A-12 contract. A member of the government's proposal evaluation committee commented on the disparities between the Northrop

bid and the McDonnell Douglas/General Dynamics bid, explaining that McDonnell Douglas and General Dynamics have "minimal experience and may not know what they're getting into." (Ex. 4023.) Eleanor Spector, commenting on the wide price disparities, stated that, "Northrop has had experience with low observables and McDonnell/GD have not so it could be the Northrop estimate was more realistic." (Memorandum from Eleanor Spector to Under Secretary of Defense for Acquisition, App. 35,129-30.)

The government possessed superior knowledge with respect to how long it would take to develop this unusual type of aircraft. At the time of bidding on the A-12 (described by Secretary Lehman as a "mini B-2"), the government was acutely aware that the B-2 had experienced substantial schedule slippage from the schedule originally predicted. Northrop had originally predicted a time to first flight on the B-2 similar to the one McDonnell Douglas and General Dynamics predicted on the A-12. But, by the time of the A-12 bidding, the B-2 planned time to first flight had been revised to about 5 years. Without access to this directly relevant information and experience, and based on the historical data available to them, McDonnell Douglas and General Dynamics erroneously believed they could achieve a 30-month first flight schedule.

The government, however, did have this B-2 information, as well as information from other classified programs, and knew that the contractors could not achieve first flight on a 30-month schedule. Among other things, Northrop told the government

that the proposed 33-month schedule was inadequate because of increased design, tooling manufacturing and assembly span times associated with the unique ATA, as compared to those for a more conventional aircraft. Armed with superior knowledge and a multi-billion dollar headstart, Northrop's bid was still 20% longer to first flight than the McDonnell Douglas/General Dynamics' bid. The government did not share this information regarding the necessary development time with McDonnell Douglas and General Dynamics, warn them of it, or otherwise protect them from their lack of this vital information before accepting their bid.

The government possessed superior knowledge regarding weight, weight estimation, and weight penalties associated with the production of a composite, thick-wing, very low observable, flying wing aircraft. The government failed to share that information, warn the contractors or otherwise protect McDonnell Douglas and General Dynamics from entering into a contract that was, unbeknownst to them, impossible to perform. Among other things, the government knew that there was a significant estimating penalty associated with a very low observables flying wing aircraft. With its experience from other classified programs, which included the B-2, Northrop calculated that this was at least a 9.4% penalty.. The government also knew that a contractor lacking experience producing a very low observable flying wing aircraft could not accurately predict the weight for this unique design. The B-2 program experienced very similar weight growth to

that later experienced by McDonnell Douglas and General Dynamics. The government knew this history and knew that McDonnell Douglas and General Dynamics did not have the most relevant weight-related data when it bid for the A-12.

Before contract award, the government also possessed other information from classified programs, including the B-2 program, concerning the development of a very low observable aircraft that the government was obligated to share with the contractors. Lacking this information, the contractors incurred expense and delay in repeating research and development on low observables technology that had been done on other government programs.

(b) Having not been provided B-2 information pre-contract, the contractors attempted to establish a process for post-award exchange of information with the B-2 program in 1988. The contractors' position with respect to the 1988 "offer" is contained in the Declaration of Albert P. Farr, III, Jan. 27, 1994, Pars. 12-16. *See also* Declaration of S. Keith Jackson, Jr., April 29, 1992, Pars. 13-16. However, because the contract had already been awarded, such information exchanges could neither address nor eliminate the impossibility of A-12 development within the cost and schedule constraints of the contract. The contractors required a general understanding, before contract award, that the development of a very low observable flying wing aircraft would be fundamentally different from development of a conventional aircraft, just as

development programs for supersonic and subsonic aircraft had been different. The contractors needed to know that their pricing, scheduling, and weight prediction methods, based on extensive experience with non-stealthy aircraft, were inapplicable to A-12. The contractors contend that, in order to discharge its duty attendant to possession of superior knowledge, the government was required to act before contract award. The government instead stood silent and, without warning, locked the contractors into a fixed price contract that could not be met. The contractors further contend that the superior knowledge duty was borne by the government, not by Northrop or the Northrop B-2 organization.

(c) The contractors have not yet made a final selection of the fact witnesses they intend to call regarding these issues. We believe that the list of potential witnesses with knowledge about these issues include: Dudley Cate, Rear Admiral Jeffrey Cook, Pike Farr, Keith Jackson, John Lehman, William Miller, and Richard Rumpf.

(d) At present, the contractors are considering whether to call expert witnesses regarding these issues. If the contractors decide to call any such experts, they will notify the government in a timely manner.

(e) At present, the documents the contractors intend to rely upon include the documents identified in response to Contention Interrogatories Nos. 7(f) and 8(d) and the following:

1. (10/90) OSD CAIG Report on the Navy A-12 Program (206//00234-93).

2. (5/20/85) Memo to Bravery Program Manager re: Special Programs Access (208//0697-85).

3. Operational Requirements.

4. Northrop Proposal, Technical Report 1, BAFO.

5. Northrop Proposal, Technical Report 4.

6. Northrop Proposal, Technical Report 27.

7. Northrop Proposal, Technical Report 22, Level 4, Survivability.

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,	)	
Plaintiffs,	)	No. 91-1204C (Judge Hodges)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DECLARATION OF JEFFREY A. COOK

1. My name is Jeffrey A. Cook. I am a Captain in the United States Navy presently serving as the AFX program manager. I have a master's degree in Aeronautical Engineering from North Carolina State University.

2. I became involved in the A-12 program in October 1987, when I began working closely with the then-assigned class desk officer in preparation for assuming class desk duties. I became A-12 class desk officer in February 1988, and held that position until November 1990 when I became the prospective A-12 program manager.

3. As class desk officer, I was responsible for ensuring that relevant technical expertise from the Naval Air Systems Command was available to the Navy's A-12 Program Office. I was the Navy's chief engineer responsible for monitoring the A-12 contractors' technical performance. The contractors' chief engineers for the A-12 Program, Keith Jackson and Pike Farr, were my principal industry counterparts. I met with them frequently.

4. As class desk officer, I sought to make available to the A-12 contractors relevant technology developed in the B-2 and F-117 programs. I began these efforts in the spring of 1988, when I arranged to be read into the B-2 program, along with another officer assigned to the class desk, CDR Bud Jewett. In mid-1988, Bud Jewett and I interacted with the Air Force's chief engineer on B-2, John Griffin, and his deputy Jim Longley. Together we planned to arrange a meeting between a core of Government engineers, a Northrop core, and a GD/McAir core for the on-going exchange of technical ideas between the A-12 and B-2 programs.

5. One of the first obstacles we faced in executing this plan was GD/McAir's refusal to get in the same room with Northrop engineers to discuss technical issues. Pike Farr was the principal opponent to meeting with Northrop. I distinctly remember him stating to me that McAir recently had had a bad experience with Northrop and would not meet with them for purposes of technology transfer.

6. Instead of meeting in person with Northrop engineers, Pike Farr and Keith Jackson generated an informal list of areas of interest, which they provided to me. But Jewett and I then conveyed their written list of questions to John Griffin and Jim Longley, who had been read into the A-12 Program for this purpose. Griffin and Longley in turn passed the list to Northrop engineers (who also had been read into A-12), and Northrop provided documents and other information they believed to be relevant.

7. I do not recall all of the technical questions raised by the A-12 contractors in the fall of 1988. To the best of my knowledge, the A-12 contractors did not ask, then or ever, about weight estimation, weight growth, or weight reduction in the B-2 program.

8. Northrop prepared information addressing the A-12 contractors' areas of interest and provided it to Griffin. I then brought Pike Farr and Keith Jackson to Wright Patterson where Longley, Griffin, and I spent an entire day reviewing with them the Northrop information.

9. This technology transfer arrangement also included the transfer of technical information from A-12 to B-2. Northrop provided its list of areas of interest to Griffin, who gave it to me to provide to the A-12 contractors. I took the GD/McAir information and met with Northrop engineers to complete the exchange.

10. In my view, this was not an effective way to conduct a technology transfer. I continued to encourage Pike Farr and Keith Jackson to agree to face-to-face technical discussions with Northrop engineers.

11. In early 1990, Keith Jackson and Pike Farr finally agreed to participate in face-to-face technical discussions with Northrop. In about February 1990, industry and Program Office representatives from the A-12 and B-2 programs met in Los Angeles for a technical exchange. Pike Farr, Keith Jackson, and Air Force and Northrop representatives were present. Northrop was represented at this meeting by its chief engineer, John Cashen, and 10 to 15 other engineers.

12. At this first set of meetings, GD/McAir's areas of interest all focused on low observable technology. GD/McAir did not raise any questions concerning aircraft weight or composite manufacturing, and those issues were not discussed.

13. Two major areas were raised by GD/McAir engineers in Los Angeles. First, they asked about flush mounted air data computers and how they were performing on the B-2. Conventional aircraft use pitot probes. These do not work in low observable aircraft, which must measure air pressure using a flush mounted system to preserve the aircraft's signature. Northrop was the leader in this area.

14. The second major issue raised by GD/McAir involved low observable antennas. There were a number of antennas on the A-12, including the multi-function antenna. These antennas were a key topic.

15. This meeting in Los Angeles was the only face-to-face technology transfer meeting between B-2 and A-12 engineers that I attended. At the end of this meeting, there was a general agreement that there would be future technical meetings at a lower level. I do not know whether these follow-on meetings were held.

16. Despite my efforts to facilitate meaningful technology exchanges, the contractors never pushed to get information from the F-117A program. They considered the F-117 program much less relevant than B-2, and their interest in F-117 related principally to how well that aircraft held up in testing and operations. At the Navy's urging, they were read into F-117A and did get information from that program in 1989.

17. I first learned of the contractors contention that the Navy failed to share relevant technology when I saw their claim in November 1990. I was stunned. I thought we had gone to great lengths to arrange for technology transfer and that any delays in the process were caused by GD/McAir's hesitations. As part of the claim review process, MAJ Jim March researched the technology transfer events that had occurred during the A-12 Program. A copy of his summary is attached. While I no longer

have a clear memory of precise dates and people present at all the meetings described, his summary appears to be accurate, at least as far as it goes. By this, I mean if anything it is probably understated in terms of the technology transfer that occurred. The contractors' chief engineers indicated to me they were working with CAPT Day who is the director of the Low Observables Technology Directorate.

18. During the summer of 1988, I learned the contractors had completed a study that projected the aircraft as then designed would weigh 4071 pounds in excess of the guaranteed weight. I was extremely concerned and, over the next 14 months, repeatedly sought assurances that the contractors would satisfy their weight guarantee. In response to these concerns, the contractors repeatedly advised me that, although the weight guarantee was challenging, they would meet it. They sought to do this by redesigning the aircraft and by experimenting with the new technologies. Even while they reconfirmed their commitment to meeting the weight guarantee, the contractors' weight projections steadily increased.

19. In about December 1989, the contractors assured me projected weight growth finally had been arrested and indicated a willingness to submit modifications to weight-related specifications to reflect the then-current projection. I agreed in theory to support such modifications once I was convinced weight growth truly had been arrested.

20. The contractors never did submit a proposed specification change notice with regard to

weight related specifications. Instead, their weight projections steadily increased over the next three months and then jumped dramatically in April 1990. The contractors sought to lower their weight projection through further redesign and experimentation. By June 1990, these weight reduction efforts had decreased the projected design weight by 1,000 pounds, although by termination most of this weight savings had been eroded by continued steady weight growth.

Pursuant to section 1746 of title 28, United States Code, I hereby declare under penalty of perjury that the foregoing is true and correct.

/s/ JEFFREY A. COOK
JEFFREY A. COOK
AFX Program Manager
Naval Air Systems Command

Executed this 21st day of December, 1993.

Page

(2) contemplated doing a bottoms-up weight estimate?
(3) A. ( ) Yes.
(4) Q. ( ) And what was - what do you recall
(5) were the contractors' intentions regarding the
(6) performance of a bottoms-up weight estimate prior to
(7) award?
(8) A. ( ) Well, it's been 15 years, so I don't
(9) recall the specifics of it. But I know that we did
(10) intend to estimate the weight of the aircraft as
(11) accurately as we could before contract award.
(12) Q. ( ) And it was your understanding that
(13) it would be more accurate to estimate the weight of
(14) the aircraft prior to award with a bottoms-up weight
(15) estimate?
(16) A. ( ) The language "bottoms-up weight
(17) estimate." I'm not real familiar with that, and that
(18) may not have been my words that appear here in this
(19) document. But the most accurate way to estimate the
(20) weight of an aircraft would be to specifically
(21) design parts. And then when you knew the volume of

(22) the part and density of the material of which the

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(1) part was made, to multiply the volume times the
(2) density, and then you have the weight. That's the
(3) best way to do it. And ideally, that's - that
(4) would have been our objective.
(5) Q. ( ) And specifically, had the
(6) contractors contemplated, prior to award, performing
(7) that type of, I won't put words in your mouth to
(8) describe that, weight estimating methodology you
(9) just described prior to award?
(10) A. ( ) We contemplated it.
(11) Q. ( ) Did you, in fact, perform that type
(12) of weight estimate prior to award?
(13) A. ( ) No, we didn't have the time and
(14) money to do that.
(15) Q. ( ) Was it possible for the contractors
(16) to perform that type of weight estimate prior to
(17) award?
(18) A. ( ) Not within the time and money
(19) restrictions that we faced at the time.
(20) Q. ( ) But absent the time and money
(21) restrictions that you faced at the time, it was
(22) possible for you to conduct that type of weight

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(1) estimate prior to award?

A. ( ) Of course.
Q. ( ) And you knew that it would have been preferable to conduct that type of weight estimate prior to award?
A. ( ) That would have been the most accurate weight estimate that we could have produced at that time.
Q. ( ) If I could turn you to page Fox 12 at the top of the page, there's a paragraph that reads "as we got into the detailed part of the program, it took us maybe six months of that kind of work to figure out that the weight was bad," and there's an ellipse, "and it's not very productive from a scientific standpoint to do two or three rims and a spar and do the analysis on it." Do you recall any discussions along the lines of the subject matter in those notes there?
A. ( ) No.
Q. ( ) Did the contractors, in fact, perform a rough order of magnitude weight estimate

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after award of the FSED contract?
A. ( ) Can you ask that a little bit more specifically? What type of estimate are you talking

about, Patricia?
Q. ( ) Rough order of magnitude estimate, specifically using target weights. Did you conduct
that type of weight estimate after award of the
FSED?
A. ( ) Target weights?
Q. ( ) Yes.
A. ( ) What's a target weight?
Q. ( ) I'm no engineer.
A. ( ) Well, I'm puzzled by your question.
Q. ( ) Do you remember any - do you
remember the contractors conducting a grassroots
weight estimate during 1988 after award?
A. ( ) What's grassroots?
Q. ( ) Do you remember assigning target
weights during 1988?
A. ( ) The terminology you're asking me
about, I'm just not familiar with.
Q. ( ) All right. Well, do you remember

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conducting the type of estimate that you just
described in lieu of the term "bottoms-up estimate"
used in these notes? And we can go back in the
transcript, and you did describe a weight estimate
methodology. Do you recall -
A. ( ) You mean whereby you design the
part, you know the volume of the part and you

know
the density of the material? Do I recall doing that
type of an estimate?
Q. ( ) After award.
A. ( ) Yes.
Q. ( ) When did you do it after award?
A. ( ) We were able to accomplish that in the summer of 1988, early summer of 1988. I believe
June of 1988.
Q. ( ) Do you recall the results of that type of a weight estimate?
A. ( ) Yes.
Q. ( ) What were the results of that weight estimate?
A. ( ) The results of that weight estimate were that we were able to predict that the airplane

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would be heavier than we had proposed it would be,
heavier than the number that was in the spec.
Q. ( ) Do you recall the magnitude by which the weight would have been heavier?
A. ( ) About 4000 pounds.
Q. ( ) Absent the time and money restrictions to which you referred, was there anything that prevented you from learning that the results of that weight estimate prior to award?
A. ( ) No.

(11) Q. ( ) If I could turn your attention to
(12) page Fox 13. Down at the bottom of the page, second
(13) to last paragraph, the notes read "out of the design
(14) change efforts we did submit design spec change
(15) notices, which were approved and contractors were
(16) paid for that. It was either the IDR or the PDR."
(17) Do you recall discussing the IDR or PDR
(18) with Dr. Fox?
(19) A. ( ) No.
(20) Q. ( ) But do you recall that as a result
(21) of the IDR and PDR, that the contractors did
(22) submit proposed specification change notices?

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(1) A. ( ) No.
(2) Q. ( ) You don't recall that?
(3) A. ( ) No, I'm sorry, I don't
(4) Q ( ) And you don't recall that there were
(5) any contract modifications that arose from the IDR
(6) or PDR?
(7) A. ( ) I don't specifically recall any.
(8) Q. ( ) Do you recall the contractors being
(9) paid as a result of the IDR or the PDR?
(10) A. ( ) I believe they were.
(11) Q. ( ) And do you recall the circumstances
(12) that triggered the payment of
(13) A. ( ) I believe they were billing events.
(14) Q. ( ) The bottom of the notes on page Fox

(15) 13 read "initially we had three design reviews:
(16) IDR, PDR, CDR. CDR was one big event and was
(17) roughly 18 months after contract award."
(18) Do you recall, sir, that the CDR was in
(19) the contract originally scheduled to occur 18 months
(20) after contract award?
(21) A. ( ) Well, I don't specifically recall
(22) it, but it sounds generally correct, yes.

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(1) Q. ( ) In fact, Critical Design Review did
(2) not occur 18 months after contract award; is that
(3) right?
(4) A. ( ) It was split up into separate
(5) events.
(6) Q. ( ) Turning to page Fox 14, the notes
(7) read "we did IDR and we did some spec changes and
(8) made some agreements, and we negotiated what we had
(9) agreed in IDR. We had agreements, we got
(10) liquidated, we got paid."
(11) Do you recall having any discussions with
(12) Dr. Fox specifically about this IDR process by which
(13) you had agreements -
(14) A. ( ) No, I don't.
(15) Q. ( ) There were liquidated payments -
(16) A. ( ) No, I don't.
(17) Q. ( ) "And we negotiated a zero contract
(18) mod in which we got things that were in

scope, some
(19) out of scope, and at the end of the day. They said
(20) here's the contract mod, and you may have not gotten
(21) everything you want but here is the bulk of what we
(22) agreed to in design review."

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(1) You do agree that there were contract mods
(2) that arose out of the IDR?
(3) A. ( ) I can't remember what they were. I
(4) don't believe this is a record of my - of what I
(5) may have said in this conversation. And I don't
(6) recall what they were.
(7) Q. ( ) Do you recall that this was - I
(8) don't think we sufficiently established the
(9) foundation for this conversation. Do you recall
(10) that this was a conference call involving yourself
(11) and these other gentlemen, or did you speak
(12) individually with Dr. Fox?
(13) A. ( ) I expect that what it says here is
(14) probably correct, where it says it's a conference
(15) call.
(16) Q. ( ) What specifically did you say during
(17) this conference call?
(18) A. ( ) Well, I can't specifically remember
(19) which of these comments were mine.
(20) Q. ( ) Do you generally recall any topics
(21) that you discussed with Dr. Fox?

A. ( ) Actually, I don't generally recall
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the phone conversation, no. So my answer is no.
Q. ( ) Do you recall generally any of your conversations with Dr. Fox?
A. ( ) Well, during the couple of months that he's been working with us, generally I've talked to him about the program a few times. Beyond that, I can't recall the specifics of it.
Q. ( ) What have you told him about the program?
A. ( ) I can't recall the specifics, but in general, I've shared with him general information about the program.
Q. ( ) Anything in specific?
A. ( ) I can't think of anything specific.
Q. ( ) Have you discussed the design review process with Dr. Fox?
A. ( ) I'm sure I have, but I can't recall the specifics of it.
Q. ( ) Well, let's turn our attention to the second paragraph on page Fox 14. "1989 it became apparent that one big CDR was not particularly helpful to the program. Billing
Page 298
events. Initially they were not going to give us anything between go ahead and first flight except CDR. Then they added PDR and IDR. Then in 1989, it

(4) behooved us and the Navy to fracture CDR into four
(5) events, and that was CLIN 3. So CLIN 3 went from

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

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MCDONNELL DOUGLAS CORP. and
GENERAL DYNAMICS CORP.
Plaintiffs,
v. No. 91-1204C
JUDGE HODGES

UNITED STATES OF AMERICA
Defendant.

Courtroom 4, Room 501
National Courts Building
717 Madison Place, NW
Washington, DC

Monday
April 23, 2001
The parties met, pursuant to notice of the Judge, at 10:10 a.m.
BEFORE: HONORABLE ROBERT H. HODGES, JR.
Judge

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MR. SNEE: The third and final topic that I wish to address, Your Honor, is one I call the logical outcome of the Court's original analysis. What I mean by original analysis, I'm referring to your decision of December 1996. That's the one you just questioned me

about a few minutes
ago, the sham analysis. I put that in quotes down there. I
want to spend a minute or two on that.
But I have read that opinion. I hope I
understand it. I've read it pretty carefully. What I want
to do is just spend a couple of minutes and say, well, what
if you agree with me that the record at least ought to be
complete, to the extent it ought to be complete, that we do
that exercise, what if you conclude that having received all
that evidence into the record, nevertheless, you still
conclude that your initial decision was correct; that you
can't decide these issues fundamentally at the end of the
day?
First of all, we've avoided a remand, because the
record is complete. The first thing, what is the
consequence of that? As a preliminary matter to all this
stuff -- and I believe the Court would agree with this --

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it's well established in case law that the government may

not be penalized for an invocation of the state secrets assertion. That's most recently, again, stated in Monarch Our concern is that although I don't think that the Court's December 1996 opinion in any way was intended to penalize the government, I do believe that in effect it had that effect. Let me see if I can get to my example this way.

First of all, you only get to this if you assume the government would lose the default case in your termination for convenience setting, and you decide the record is complete, but you still can't decide if there are loss adjustment claims connected. What you decided on, I believe, in the December 1996 opinion was this. The government in a T for C setting wants to apply a loss adjustment to the contractors' incurred costs. That's what the contract says. That's what the FAR says. That's all cogently, clearly explained in your December '96 opinion.

The contractor is going to say, well you can't apply that loss adjustment to the government because I have some equitable adjustment claims. If those equitable adjustment claims were valid, then my contract price would be increased and I wouldn't be in a loss position. And you concluded, at least as the claims were then stated, not as they're in contention, but because they

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seem to talk a lot about technology, that those claims couldn't be litigated. The Court could not safely litigate the equitable adjustment claims related to superior knowledge. And you concluded that it would be a sham to apply the loss adjustment if the contractors were effectively deprived of their defense of equitable adjustment costs. That's what I think -- that's why I use the word "sham". That's what I mean. It's kind of this pingpong. They say they've got a defense that's

closely tied to the
superior knowledge claims, but I can't fully litigate that.
Thus, I can't decide their defense. Thus it would be unfair
to let the government apply this to loss adjustment.
If that analysis is correct, Your Honor, just
playing it out, the logical extension of that analysis is
that the plaintiffs also cannot get a judgment for their
full incurred costs, because the government's claim of loss
adjustment is our defense to their claim for full incurred
costs.
If it's a sham to say, well, can't litigate
claims, therefore, the government were not going to apply
the loss adjustment because that would be a less-than-full
trial, the government would then say, well, if I'm deprived
of my loss adjustment defense in the same way and then the
contractors can't be entitled to a judgment for their full

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incurred costs.
The logical extension of your analysis from
December 1996 would simply be that both

parties would walk
away. The contractors are not entitled to a judgment for
more money. They've been paid $2.6 billion to that point.
But if it's unfair to litigate their claims because the government can't apply its loss adjustment, if
the government is deprived of its loss adjustment, the
government shouldn't be subject to the full incurred costs.
It should simply be that the contractors are entitled to no
more money.
Arguably, perhaps the government is not entitled
to any return of the money. It may literally work out to be
kind of a walk-away situation. But that would seem to be the
logical extension of that analysis.
Alternatively, what the Court concluded is that --
-- here's a sort of different prism to look at the same issue
-- the Court concluded that you couldn't decide equitable
adjustment claims because of its close connection with state
secrets as it was then stated, and yet as the contractors
admit, they were in a loss position but for

their claims.
So that if they are given a judgment again, of a
full incurred cost, then the net effect is they would be
granted all of their claims even though we're saying we're
not litigating the claims.

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So again, if you look at it through that prism,
the only possible outcome of your 1996 opinion it seems to
me would be to order that neither side can recover from the
other. That's not the government's position. That's not
our position today.
We believe, as we would indicate here, that the
normal position with respect to what do you do in the event
of a state secrets invocation is simply remove the evidence
from the case. In that case, the one thing on which the
privilege has been asserted, the Court decides based on the
pools of evidence that are available.
JUDGE HODGES: You might recall that I tried to
resolve this case on that very basis many,

many times.
Everyone just walk away; this case can't be tried.
I argued that to General Hunger and to Mr.
Shebraia and Mr. Honignan. Nobody would listen. We've come
full circle now. We think we should all walk away. I agree.
MR. SNEE: I'm clearly stating, Your Honor, that
from the United States' position with respect to this case,
if the Court continues to adhere to its December 1996
analysis, that would seem to me to be the logical outcome of
its analysis.
JUDGE HODGES: Here's the thing, though. The
sham legally I think if we're talking about Molerio, the
sham that they referred to there was the fact that the Court

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knew information that was the subject of state secrets that
would have made a difference in the holding at that trial.
If I'm thinking about the right case, it was a
jury trial. And the judge was given some information that

was a state secret. He knew that given the case without that information, it would have gone the wrong way. That's what he talked about. And the Circuit agreed, which is not exactly -- it's not the sort of sham you're talking about here. You've got these three claims that I've thrown out of the case. The sham part is the reason I've thrown them out of the case, because we can never get to the bottom of it.

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MS. MAYNARD: Good morning your Honor. The government's motion for reconsideration of your March 1st order should be denied First and foremost, the conclusion that you reach in your order is correct. As you recall, you removed from

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this case issues involving superior knowledge, loss adjustment and profits, and your order reinstated an order

that was based on a full opinion that you wrote in 1996, and that opinion is based and supported by well established state secrets precedents. In that opinion, you relied on the same types of things that other courts have relied upon to remove issues entirely from litigation. You relied on the fact that the evidence over which the state secrets provision has been invoked and which has been denied to the contractors in discovery is central to the issues to be decided in our superior knowledge defense, both to the government's loss adjustment claim and to the government's claim that we were in default on this contract. You relied on the fact that the parties, if there were a trial on this issue, would have every incentive to probe as close to the secrets as possible to try to make out their case. And you relied on the fact that based on their years of discovery and discovery disputes that have been before Your Honor and the fact that should

you, that if
21 there had been evidence in discovery, including evidence by
22 the government where parties had knowingly or unknowingly
23 stepped over the line into the information that was
24 protected, that those types of incidents had occurred. And
25 you concluded that if a trial on these issues was to be

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1 held, it would be impossible to ensure the safety of the
2 material covered by the invocation.
3 You also relied on these considerations such as
4 those in Molerio, before the trial without the information,
5 and under the conditions that the contractors would be put
6 under in trying to make out their defense, that the result
7 was likely be an unreliable one.
8 Those are the same types of considerations that
9 other courts have used to take issues out. Most notably,
10 the Fourth Circuit in Farnsworth TNA and in Fitzgerald, the
11 D.C. Circuit in Molerio, and other courts, including the
12 Second Circuit and the Fifth Circuit in

Bereford and
13 Zuckerman have noted those factors.
14 So your opinion is totally supported by state
15 secrets precedent. And for the recent case from the federal
16 circuit, Monarch. It's not in any way to the contrary. That
17 case, for one, as you noted, is a very different case from
18 this case. And they did not, as government counsel
19 contents, they did not send it back to Judge Bruggink to
20 hold a trial. They sent it back to Judge Burggink to let
21 the plaintiffs have very limited discovery from
22 nongovernmental sources.
23 So all they held was that Judge Bruggink should
24 have let the discovery continue slightly further before
25 deciding. They did not have a fact have a trial. They did

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1 not send it back to have evidentiary hearing of the claims.
2 And that's what the government is seeking here.
3 In addition, in Monarch, Judge Bruggink hadn't
4 found that the plaintiffs had made a prima

facie case. But here, based on the briefing and evidence attached to that briefing and the things this Court has seen and heard, you have already found that the plaintiffs can make out a prima facie case of a superior knowledge defense. This case is not in the same posture as Monarch. You have had years of discovery and years of overseeing this case. We have had actual incidents of the invocation, the material covered by the invocation being revealed in discovery when it wasn't supposed to be. Those types of things hadn't happened in the Monarch case. So your decision to remove these issues from the litigation, these fully supported by precedent, is not contrary to the federal circuit decision.

[BLANK]

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Contrary to what the government argues, our claim is not narrowed. Our claim is the same claim that we made in our complaint and our claim, in fact, the fact that the government has had to reinvoke the state secrets privilege in the course of our taking discovery since remand on our superior knowledge defense and on our impossibility defense denies any notion that our claim is somehow narrowed. Your Honor hit right on the head when you asked Mr. Snee, isn't this really about technical issues, and yes it is, whether you frame it as weight schedule and cost it all comes down to what did the government know prior to award about low-observable programs and the technical issues associated with low-observable programs. Virtually every aspect of the A-12 was driven by the low-observable requirements, the shape of the plane, the weight of the plane, how much it was going to cost to build the plane, how long it was going to take,

what kind of
problems we encountered, things that we had to work around,
how long it would take to work around those issues, all
those things were driven by the low-observable nature of the aircraft.
aircraft.
It is highly relevant to our claim. Everything
that the government knew from the low-observable programs
prior to award, and we have been seeking discovery into
that, and we have been continually blocked from discovery.

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We have also been continually blocked from
discovery into any mechanisms that the government had to
share information from these other low-observable programs.
I'm not able to say more about that in this
setting, but I have been able to say that we have been
consistently blocked from receiving full discovery in those
areas.
Although the government suggests that we have had
full access in the B-2 program, in recent depositions, our

attorneys have been informed by Air Force security officers
that we are not being given access to all B-2 information
and that there is B-2 information that even our B-2 cleared
attorneys cannot have.
Furthermore, just several days ago, Mr. Churchill
was stopped by Air Force Security for questioning the
government's purported expert on program management, Mr.
Canoe, who is a former B-2 program manager.
As you'll recall, we've made a separate motion to
exclude Mr. Canoe.
Mr. Churchill was trying to propound questions
relating to Mr. Canoe's experience in the B-2 program, and
he was stopped last Thursday and Friday from asking certain
questions. Just as a side note, the Exhibits on our Exhibit
list that go to the B-2 weight growth are specifically
anticipatory to rebut Mr. Canoe.

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We are not trying to try our superior knowledge
issue defense in contravention of this

Court's order. The
only reason we put them on there is because in order to
effectively rebut Mr. Canoe, we're going to need to get into
the B-2 information.
So the result that you have reached. Your Honor
is fully supported by the state secrets precedent. Our
claim is not any narrow. Indeed, I just want to highlight,
for the Judge, a couple of things about our claim.
Our claim is the same claim that the government
told this Court in 1993 and 1994 could not be litigated.
If we could put up on the overhead, Pete?
(Slide.)
This is a pleading the government filed in 1994.
Next page.
(Slide.)
The government told this court that there was no
separate justiciable non-privileged portion of the superior
knowledge claims that plaintiffs could pursue in this
action.
Then the Court told the Federal Circuit the same

thing, Your Honor. The Court told the Federal Circuit – If you could put up C?

(Slide.)

– this is a portion of the Federal Circuit's decision where it relates the government argued to them on appeal This is Federal Circuit at pages 1329 carry over to 1330

The government argues that contractor's superior knowledge and reasonable profits claims were properly removed from litigation because they jeopardized state secrets

So the government told the Federal Circuit, as recently as 1998, that these claims could not be tried And the only reason that they are arguing differently today is based on this fallacy that somehow our claim has narrowed.

I'm here to strenuously object to that characterization of our claim. Our claim has not narrowed.

What the government is seeking to do, Your Honor, is to have a trial on the superior knowledge and

impossibility issues, a one-sided trial they're seeking to have a trial with only their evidence. We have been blocked in discovery from getting the evidence that we seek to defend ourselves from the government's default termination and to defend ourselves from the government's loss adjustment claim. We have been continually stopped, both in depositions and, as you know, you are aware the government invoked the state secrets privilege over certain questions that we asked

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The government wants to force us to have a trial where we have to have both of our hands tied behind our back and they put in our evidence. There's two things wrong with that. One, that extremely prejudices us. We believe that it's a violation of due process to go forward with a trial where the government has invoked the state secrets privilege to remove information relevant to our defenses and yet then goes to trial to try to impose

forfeiture upon our client.
And two, we believe that doing so, we'll run the
very risk that you are afraid of. We'll run the very risk
that your order is meant to protect against.
We will, and we have an ethical obligation to our
clients to protect them against this forfeiture, which we
think is wrong, and we will have every incentive to come as
close as we can to whatever is it that's covered by the
state secrets invocation.
As Your Honor is aware, we are not privy to
exactly the coverage of the state secrets provision. So
this trial that the government argues won't take very long
is actually going to be a trial with only that evidence,
and we will have every incentive to probe as close as we can
to whatever it is that's been removed so that we can try to
defend ourselves, even though, as I said, it will be with

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our hands tied behind our back
The government basically wants to have

its cake
and eat it too. They want to take out the evidence that we
need for our defenses and go forward with the evidence that
they've got and the evidence that they've been willing to
share with us

* * * *

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

* * * * * * *

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION,

Plaintiffs,

v.

UNITED STATES OF AMERICA,

Defendant.

* No. 91-1204C

* Filed: April 27, 2001

* * * * * * *

ORDER

Defendant has asked that we reconsider the March 1 Opinion and Order "removing the issues of superior knowledge, loss adjustment, and profit from trial, and to adduce, at trial, a complete factual record regarding all issues and including all pertinent available evidence." We cannot grant this motion because it is not possible to obtain a "complete factual record' in the circumstances of this case.

The Executive Branch has warned us repeatedly that issues involving superior knowledge

cannot be litigated safely. Citations to these declarations of government officials authorized to make such determinations are included in the March 1 Opinion and Order and in *McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 270 (1996). If these references do not provide sufficient evidentiary basis to support the Court's conclusion in this regard as defendant charges, we will try to fashion a means of addressing that problem with the Federal Circuit at the appropriate time. Meanwhile, a review of the case law in this area does not suggest that a court should enter judgment based on incomplete evidence. Such a procedure is particularly inappropriate when the court is aware of information that is necessary to a fair judgment but cannot use such information. *See Moleiro v. FBI*, 749 F.2d 815 (D.C. Cir. 1984).

The Government argued to the Federal Circuit that superior knowledge and reasonable profits claims "were properly removed from litigation because they jeopardized state secrets . . . ." *McDonnell Douglas Corp. v. United States*, 182 F.3d 1319, 1329-30 (Fed. Cir. 1999). Thus, at least two of the interrelated superior knowledge issues could not be litigated safely, according to defendant. The Circuit did not address the third issue concerning defendant's loss adjustment claim because that claim will arise only if this court again converts the termination for default to one of convenience. *Id.* at 1330.

The Federal Circuit did not state that this court was obligated to issue a judgment on an incomplete record. It did not determine that this

court abused its discretion in removing superior knowledge issues from the case when it made a factual finding that such issues could not be litigated safely in light of national security considerations. The Circuit left this court free to reconsider its position on remand "[b]ecause of the passage of time and of possible intervening developments . . . ." *Id.* Evidently the court thought that some of the programs affected by this lawsuit would have been declassified by now, or become less sensitive.

Neither the passage of time nor intervening developments have lessened the risks that prompted us to act in the first instance. Our findings of fact in that regard are set out in the March 1 Opinion and Order.

In summary, we cannot permit litigation of issues related to superior knowledge because of the resulting risks to national security. These risks are documented in the declarations of Secretary Peters, Secretary Rice, General McPeak, Secretary Donley, and others. *See McDonnell Douglas*, 37 Fed. Cl. at 281-84. They are documented in numerous opinions and orders of this court since 1991. They are documented by other information that can be made available to the Federal Circuit if necessary. If this court were to permit trial of superior knowledge claims using only information obtained from the B-2 and F117 programs, we would be forced to enter judgment based on evidence that is incomplete and misleading. *See Molerio*, 749 F.2d at 825.

Trial of this case begins at 10:00 a.m. on May 7 and 9:00 a.m. thereafter until June 29. The court

will not meet on May 28 or June 4-8. The time will be evenly divided between plaintiffs and defendant. Mr. Lewis is excluded as an expert witness. *See* Transcript of Hearing on April 23, 2001. All other motions that were pending and not listed on the April 23 proposed agenda and status report are moot and therefore denied.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

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IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION	)	
and	)	
GENERAL DYNAMICS CORPORATION.	)	
Plaintiffs.	)	No 91-1204C
v	)	
UNITED STATES OF AMERICA.	)	
Defendant.	)	

VOLUME II
Courtroom 4
National Courts Building
717 Madison Place NW
Washington, DC
Monday. May 7. 2001

The hearing commenced, pursuant to notice of the
Judge. at 2:00 p.m.

BEFORE: HONORABLE ROBERT HODGES
Judge

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APPEARANCES (CONTINUED)

For the Defendant
BRYANT SNEE, ESQ.
ROBERT E. KIRSCHMAN, JR.. ESQ.
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ALSO PRESENT:
JOHN HUGHES
MIKE MACISSO
WOODY GIBSON

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(Dicussion off the record.)
Whereupon,
JOHN P. LAMERS
was called as a witness and, having first been duly sworn,
was examined and testified as follows:
THE COURT: You have been briefed, Mr. Lamers, I understand by security?
THE WITNESS: I have, yes, sir.
THE COURT: Thank you very much.
EXAMINATION
BY MR. SNEE:
Q Good afternoon, Mr. Lamers.
A Good afternoon.
Q You and I have met on a number of occasions before, so I won't reintroduce myself for the record.
Mr. Lamers, you were the principal program manager for McDonnell Douglas-General Dynamics team for the ATA/A-12 program from its inception; is that correct?
A **Yes.**
Q *And you continued your association with the program throughout the entirety of the program, up until the time of its termination; is that correct?*
A Yes.

Q And since termination, have you worked for a substantial period of time in support of General Dynamics'

* * * *

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orientation tape for new employees of the program?.

A I believe I did.

Q That would have been maybe early 1988, shortly after the FSD award of the contract?

A I don't remember a date, I'm sorry.

Q Why don't we do this. What I would like to do is play what's been marked as Exhibit D3473. I take it you don't want a videotape?

MR. CHURCHILL: Thank you, Bryant.

MR. SNEE: Can we try that, please?

(Videotape played as follows:)

"Mr. Lamers: My name is John Lamers, program manager for A-12, and I want to welcome you to the program. Normally, I would be with you in person to welcome you aboard, but just to cover the fact that sometimes I can't make it, we wanted to make a videotape, have it available

and let you meet me in that way and let me talk a little bit about the program, tell you what we're doing out here.

"As with all such efforts, this program began many, many years ago and was initially a small effort in advanced programs. Actually, here in the Fort Worth division, we've been working on predecessor activity, predecessor programs, for 10 years or so.

"The program many years ago was really kind of an idea that was originally conceived by Keith Jackson, who

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is still with the program today as the chief engineer. And it was an interesting airplane in those days, because our analyses, our studies continued to show that no matter which way you looked at it, this was a very effective, very survivable airplane.

"The problem was, trying to find a customer for it. For a while, we thought the customer would be the U.S. Air Force, but as it turned out, when they finally decided

that the advanced tactical fighter had to be a supersonic airplane, this one was left behind, and there was a period of time back in the early 1980s when actually, we began to think that this would never amount to anything.

"Then along came the U.S. Navy, looking for a replacement for the A-6, and it was brought to their attention that this airplane would be an excellent candidate for that assignment" —

(End of videotape.)

MR. POTTER: Your Honor, what does this have to do with anything in the cure notice? This to me looks to be wholly irrelevant to anything in the cure notice, and I wonder what the relevance of this is.

THE COURT: I'm just putting myself in Mr. Snee's hands and assuming he's going to explain it all.

MR. SNEE: I certainly will, your Honor. And I certainly appreciate your indulgence. As I said earlier, I

* * * *

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IN THE UNITED STATES COURT OF FEDERAL CLAIMS

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION. Plaintiffs.	)	No 91-1204C
v	)	
UNITED STATES OF AMERICA. Defendant.	)	

VOLUME L
Afternoon Session
Courtroom 4
National Courts Building
717 Madison Place NW
Washington, DC
Friday, June 15, 2001

The hearing reconvened at 2:05 p.m.

BEFORE: HONORABLE ROBERT HODGES, JR.
Judge

* * * *

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APPEARANCES (CONTINUED)

For the Defendant:
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ALSO PRESENT:
JOHN HUGHES
LEONARD BALLOU
JAMES WHITE
MIKE MACISSO

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AFTERNOON SESSION (2:05 p.m.)
Whereupon,
S. KEITH JACKSON

resumed the stand and, having been previously duly sworn,
was examined and testified further as follows:

CROSS-EXAMINATION

BY MR. SNEE:

Q Good afternoon, Dr. Jackson.

A Good afternoon, Mr. Snee.

Q I would like to spend our first few minutes together talking about a little bit on the -- as Ms. Maynard did, with respect to your background. If I understood your responses in response to her questions, that you basically arrived at what was then General Dynamics Fort Worth in sort of the late 1960s period; is that correct? that correct?

A About 1966. 1967, excuse me.

Q '67, okay. And you mentioned you first spent a little bit of time in the advanced space program; is that correct?

A Yes, that's correct.

Q And then after a fairly brief period of time, you moved over to advanced aircraft program; is that correct?

A That's correct.

25 *Q And you said that you spent an amount of time as*

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1 a project engineer or senior project engineer in that
2 organization; is that correct?
3 **A Yes, yes.**
4 *Q And that you did, among other things, a number of*
5 *studies, is that correct?*
6 **A Correct.**
7 *Q And that you managed some advanced design work in*
8 *that area?*
9 **A Yes.**
10 *Q And that you managed for a period of time or*
11 *ultimately became manager of the advanced technology*
12 *portions of the advanced aircraft programs. Would that be*
13 *correct, in general terms?*
14 **A Generally speaking.**
15 *Q Yes, I don't mean literal titles, but concepts*
16 *at least with respect to that.*
17 **A Right.**
18 *Q And that you also spent an amount of time doing*
19 *conceptual studies of the various aircraft designs, some of*

which ultimately evolved into what became the ATA proposal
in this contract; is that correct?
MS. MAYNARD: Objection, your Honor. I think
that mischaracterizes his testimony. I don't believe we
got into that.
THE COURT: Well, he'll - he can certainly

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clarify his recollection of it, if he likes. If you don't
agree with the premise of the question, Dr. Jackson, by all
means, clarify it.
THE WITNESS: No, I would agree.
BY MR. SNEE:
Q You would agree with the premise?
A More or less with the premise, yes.
Q That you spent a period of time doing various
analyses of different aircraft concepts, and some of those
analyses evolved into what became the GD portion, at least,
of the proposal for what became the ATA program; is that
correct?
A Yes, by a somewhat circuitous route, but essentially, that's probably correct.

Q And that during this period of time, how early would you date that first studies that evolved into the ATA concept as it was ultimately proposed in 1987?

MS. MAYNARD: Your Honor, I'm sorry to object right at the initiation of Mr. Snee's cross, but I believe this line of inquiry all goes to the superior knowledge issues which your Honor has removed from the case. I was very careful not to get into this area with Dr. Jackson, in accordance with your order. And I believe that this is out of bounds for what you have ruled is in the trial.

THE COURT: Well, I can't tell yet that it is. I

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don't want to get into superior knowledge for any number of different reasons, but so far, I don't – I think he's merely responding so far to some of your questions on direct.

MR. SNEE: That is correct, your Honor.

THE COURT: So I'll overrule that objection for the record.

MR. SNEE: And I should say, your Honor, I am extremely mindful, I believe, as I told you in opening statement, that I believe I understand, have done my very best to abide by your orders with respect to what issues are in and what issues are out. And I can assure the Court that my line of inquiry here has nothing to do with potential superior knowledge issues in the case.

BY MR. SNEE:

Q So if we could, could we at least – my question was to try to understand when in this circuitous route would you say you first began doing analyses of concepts or programs that rolled into this ATA proposal?

A Well, if you would consider the flying wing concept, that probably started sometime in 1974.

Q Sort of the mid-70s; is that correct?

A Mid-70s, yes.

Q And that form mid-70s on, until, in fact, until early 1984, you yourself were largely engaged in conducting

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analyses and directing the efforts of others with respect to developing this concept of a flying wing attack aircraft; is that correct, sir?

A No, that's not really correct. I worked on the flying wing as one of many airplanes that I worked on. It was probably far less than half my time. I would say, you know, a quarter to an eighth of my time was spent on that particular concept. It varied from time to time as to how much I spent on it, but it was not full-time.

Q That would be a fair statement. You looked at a number of different aircraft concepts; isn't that correct?

A Yes.

Q From this – throughout this development effort. And in fact, a large portion of this – not a large portion, but some of this effort was a result of Air Force

contracts to study various attack aircraft concepts; isn't that correct?

A It was Air Force interest. In many of those studies it was company-funded money and not Air Force contracts as much. We worked with the Air Force on it.

Q Both. Portions of this work was being done by company money and portions of this work was being done as a result of Air Force contracts; correct?

A Yes.

Q Does the acronym ATS mean anything to you in

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connection with Air Force studies in, say, the 1975 to 1977 time period?

A Yes.

Q What was the ATS as it related to the Air Force contracts?

A That was the air-to-surface technology and integration study.

Q And what – could you generally describe what that study effort entailed?

A It was a study to try to look at the various advanced technologies that were being looked at at the time, and to incorporate them into aircraft of different characteristics, to see which techonologies had the most potential for future airplanes.

Q And when we're talking about "aircraft," these were principally attack aircraft concepts?

A In the ATS study, it was principally attack aircraft concepts.

Q And there were a couple, at least, of different configurations, principal configurations, that were ultimately studied in more detailed in the ATS study; is that correct?

A Yes, that's correct.

Q And one of those configurations that was studied in this ATS study was a flying wing aircraft; is that

Page 4858

correct?

A Yes.

Q And there was a non – at least one nonflying

wing, perhaps a couple more, nonflying wing; is that correct?

A Yes.

Q And the nonflying wing aircraft may have had at least some point in its – in that analysis, might have been referred to as the plain Jane, is that a nickname that sounds familiar to you?

A Yes.

Q And the flying wing aircraft that was studied also had a number over the years, a number of other nicknames; is that correct?

A Yes.

Q And those nicknames would include – or code names. I don't mean to be disrespectful. Sometimes they might be a literal security name; is that correct? Other times it might be just an in-house kind of way to refer to the design. Is that a fair characterization?

A Yes.

Q And the flying wing, you mentioned a circuitious route, this flying wing concept passed through over the

years, under the names such as Coal Pigeon, is that an applicable name?

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A Yes.

Q Sneaky Pete was another name for this evolving all-wing concept; is that correct?

A Yes.

Q Model 100 was another name for that concept?

A That's correct.

Q And while you say today that about as little as an eighth of your time was spent exploring this flying wing concept, is it not correct that this flying wing concept was under consistent consideration, from around mid-1974 up until your involvement in the ATA program?

A Yes.

Q And in fact, isn't it true that approximately around 1976, under thes concepts, I think it was perhaps a half-scale model of this flying wing was tested on a radar cross-section range?

A We did test a half-scale model, I think that was

a little later. I think the first model we tested was a quarter-scale model.

Q Quarter-scale. would htat have been around '75, '76 for the first time?

A '75-'76 time frame.

Q When do you recall the half-scale model being tested?

MR. POTTER: Your Honor, this really does seem

* * * *

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correct?

A Yes.

Q When did you first become involved in the ATA program?

A That was probably sometime in, I would guess, the summer of 1984.

Q Can you just generally describe how it is you got involved in the program?

A The Navy had been looking for new airplanes, a replacement for the A-6 was one of them. The first time I remember things related to the particular *ATA* program was

when a team from the Center for Naval Analysis came through, led by Dr. Ken Lobb, looking for ideas, particularly the use of stealth for advanced naval aircraft. We briefed him on some of our ideas.

Q One of those ideas that you briefed the Navy on was, among others, was this flying wing low observable aircraft design that I think we'll agree to call "Sneaky Pete" at least for now; is that correct?

A It wasn't called Sneaky Pete at that time, but it was that lineage, yes.

Q That lineage, fair question. That would have been about what time frame, sir?

A I can't remember the exact time frame there. I think it was probably in 1984 sometime. It may have been

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like late 1983. I'm simply not sure.

Q And so it was Mr. Lobb – I think you said – did you say Center for Naval Analysis?

A Yes, Dr. Ken Lobb, yes.

Q Dr. Ken Lobb, he was from the Center for Naval Analysis?

A Yes.

Q You understood the Navy was looking for a replacement principally for its A-6 medium attack aircraft; is that correct?

A Yes, as I remember, that's correct.

Q And one of the – in fact, needing – identifying on behalf of the Navy, the Navy identifying a need for replacement for the A-6 is very, very similar to the types of requirements analysis that you have been doing for the last seven to 10 years; it that correct?

A Yes.

Q Identifying what type of airplane do we need in the future to meet the threats of the future; is that correct?

A That's correct.

Q And when Dr. Lobb and others from CNA came and asked what ideas you have, you provided some ideas; is that correct?

A Yes.

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Q And one of those ideas was this flying wing lineage aircraft; is that correct?

A Yes.

Q And that's the idea that ultimately evolved into the General Dynamics Fort Worth proposal aircraft design on the ATA program; is that correct?

A Yes, it evolved into that eventually.

Q With more development work along the way. Is that a fair statement, sir?

A Right.

Q did there come a time, sir, in the 1983ish period, maybe, in which General Dynamics made the decision to close down the efforts, let's say perhaps before Mr. Lobb and the CNA showed up?

A Yes.

Q In which General Dynamics made the decision to close down this design effort that you had been leading for that period of time?

A Yes, they did.

Q Why did they make the decision to close down that design effort?

A Well, we had been primarily working with the United States Air force on those concepts. They had considered it very carefully and had decided to adopt what became the F-22-type characteristics, as opposed to the

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kind of characteristics shown by the airplane type that we're talking about.

Q And that would principally be this ATS study that you'd been developing, the Air Force makes the decision sometime late '70s, fair characterization, that for their F-22-type thing, they would like a faster after-burning aircraft. Is that a fair statement?

A Yes, that –

Q Supersonic, I should say.

A That probably was in the '83 time period, I would suspect.

Q It's at that time General Dynamics made the decision to no longer continue the development of the flying wing aspect under your tutelage at about that time;

is that correct?

A Yes, that's correct.

Q And it was shortly thereafter or so in which Mr. Lobb and the Navy came down to seek information with respect to that; is that correct?

A That's correct.

Q so in that respect, it's almost a happy circumstance for the company that the Navy came down seeking information relating to advanced designs that might be available; is that correct?

A I think you might get some argument on that, but

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probably so.

Q In the end you might be right, sir, but the intentions at the time were the best. is that a fair statement?

A That's a fair statement.

Q On behalf of the company and on behalf of the Navy. Is that a fair statement?

A Right.

Q Absolutely, I thought so. What I would like to do is turn, if we could, to your role in the actual ATA

program. And for simplicity, can we just call it the A-12 program, as you know, through the source selection and all that? You know it better than I do, sir, but for simplicity, let's just call it the A-12 program. What I would like to do is just put up on the screen two different charts, I hope, as what will be just a kind of simple aid. If I can read – if you can't read it, I think I can fish out a hard copy. I'll tell you, these are just organizational charts and I just want to use them for a few minutes to see if we can get reference. If we can't, Dawn – are you back there, Ms. Ericksen? Oh, I'm sorry, Tom. Excuse me. This would be found in Defendant's Exhibit D296, if it would be easier for you, Dr. Jackson. Tom, I think, should have – do you have D296, I hope? Can you read off

* * * *

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

No. 91-1204 C

MCDONNELL DOUGLAS CORPORATION
AND GENERAL DYNAMICS CORPORATION,

JUDGMENT

v.

THE UNITED STATES

Pursuant to the court's Published Opinion, filed August 31, 2001,

IT IS ORDERED AND ADJUDGED this date, pursuant to Rule 58, that the complaint is dismissed and judgment is entered in favor of defendant. No costs.

Margaret M. Earnest
Clerk of Court

August 31, 2001 By: */s/*

Deputy Clerk

NOTE: As to appeal, 60 days from this date, see RCFC 72, re number of copies and listing of *all plaintiffs*. Filing fee is $105.00.

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

* * * * * * *

McDONNELL DOUGLAS CORPORATION and GENERAL DYNAMICS CORPORATION, *

Plaintiffs, *

v. *

UNITED STATES OF AMERICA, *

Defendant. *

* No. 91-1204C

* Filed: October 4, 2001

* * * * * * *

ORDER

Plaintiffs' motions to alter or amend judgment for the most part raise issues that should be addressed to the Federal Circuit on appeal. Paragraphs 1-5 of McDonnell Douglas' brief summarize an argument that its counsel raised persuasively during trial, but it is one that the Federal Circuit has foreclosed in our view. Similarly, the Circuit has rejected the arguments in Paragraphs 6 - 10.

With regard to Paragraph 11 and following, the parties may have misapprehended the court's

ruling. We did not intend to enter a money judgment for the United States. We ruled that defendant's termination for default was proper according to the Federal Circuit's guidelines on remand. That judgment is final and appealable so far as we are concerned.

We addressed the state secret issue in the opinion. The assertions made by McDonnell Douglas in its Paragraph 16(a) and similarly by General Dynamics on pages 5 and 6 cannot be established. The parties have discussed in the past the issue of who bears the burden when the Government takes sensitive information out of a case but those discussions assumed that it was clear whom the information would have benefitted.

Plaintiffs' motions are DENIED.

/s/ Robert H. Hodges, Jr.
Robert H. Hodges, Jr.
Judge

BRIEF FOR DEFENDANT-APPELLEE-CROSS-APPELLANT

Nos. 02-5034, -5035, -5046

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

McDONNELL DOUGLAS CORPORATION AND GENERAL DYNAMICS CORPORATION,

Plaintiffs-Appellants,

v.

THE UNITED STATES,

Defendant-Appellee-Cross-Appellant

APPEAL FROM THE UNITED STATES COURT OF FEDERAL CLAIMS
IN 91-CV-1204, JUDGE ROBERT H. HODGES, JR.

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* * * *

SUMMARY OF ARGUMENT

As the contractors correctly acknowledge, this Court remanded for a determination of whether the contractors were in default of "this" contract, referring to the A-12 contract. GD Br. 4, 5, 10, 20, 28; MDC Br. 29-30. Although the contractors attempt to make it appear that they were performing "this" contract, in fact, they contend they "were building an aircraft that met the Navy's needs," according to a schedule that was not fixed, specifications that were never completely certain, and at a price that was never negotiated. GD Br. 4-5. The truth is there was not, and never was, a contract for an aircraft that simply "met the Navy's needs," and, as this Court held in 1999, the contractors' alleged performance of that task is irrelevant.

The Defense Department decided that it did not desire a new contract, and it became necessary to terminate the FSD contract. The Navy terminated the contract for default because it determined that the contractors' inability to perform the existing contract was not the Government's fault. The trial court correctly sustained this determination.

This Court previously held that, based upon the contract's default clause, the contractors were obligated to make sufficient progress so as to avoid endangering contract performance. Performance was defined by the specified contract schedule, as revised, which included delivery of the first aircraft in December 1991.

After conducting a six-week trial, the court below correctly found, as fact, that the revised schedule, including the first delivery date of December 1991, was reasonable and enforceable, and the contractors would not meet it. This failure was not immaterial; it was the essence of performance pursuant to the express terms of the contract. The trial court then correctly held that the termination for default was justified.

The contractors' failure to make progress toward achieving the specified delivery schedule jeopardized their performance of the entire FSD effort. As this Court noted, the contractors experienced performance problems from the beginning. Their inability to meet even their own manufacturing schedule had become a "show-stopper" by the time of termination.

The contractors' fundamental position upon appeal, argued for the first time in their post-judgment motions, is that the trial court should have focused exclusively upon their ability to complete the entire contractual effort as a measure of default. This new contention was rejected by this Court in 1999. This contention is contrary to the language of the A-12 contract's default clause, which this Court addressed in its 1999 decision. In addition, the case upon which the contractors now rely, *Lisbon Contractors, Inc. v. United States*, 828 F.2d 759 (Fed. Cir. 1987), involved a materially different default clause and materially different factual circumstances. Finally, even if the trial court were required to focus exclusively upon the contractors'

completion of the entire contractual effort, which was not funded at termination, the record establishes that no one in a program leadership position believed, at the time of termination, that the contractors would have delivered eight A-12 aircraft meeting the Navy's needs without a fundamental restructuring of the program and a new contract.

The record contradicts the contractors' secondary challenge to the trial court's judgment of default, which asserts that the December 1991 delivery date for the "stripped down" first aircraft was not achievable. The trial court correctly found that the revised schedule was both reasonable and specific from the standpoint of the contractors' performance capabilities at the time the Navy established the new delivery date. The contractors' arguments to the contrary are based upon their misinterpretation of the applicable standards for determining the reasonableness of a unilateral schedule.

The trial court correctly rejected the contractors' schedule waiver arguments. 50 Fed. Cl. at 319. Its decision is supported by Captain Elberfeld's credible testimony and the contractors' failure to present any evidence of detrimental reliance, a required element of waiver. *Id.*

The trial court also correctly rejected the contractors' argument that its holding precluding further litigation of the superior knowledge issue erected a bar to the court's ability to sustain the default termination. The doctrine of "superior knowledge" does not extend to classified information.

The trial court correctly addressed the superior knowledge issue in this case. After extensive discovery into other, classified programs and numerous attempts to develop a procedure that would permit litigation of highly classified matters, the trial court finally held that it could not permit the claim of superior knowledge to be litigated further.

Given this unchallenged holding, the trial court correctly applied the law when it removed the issue of superior knowledge from the case and proceeded to litigate the Government's claim that the contractors were in default and the contractors' defenses to that claim. Where, as here, there is a valid invocation of the state secrets privilege, its effect is to remove the privileged information completely from the case. The Government did not rely upon state secrets to prove its claim of default, and the contractors failed to meet their burden of proving the merit of any of their defenses. The contractors' claim that they should prevail nonetheless would impermissibly penalize the Government for protecting national security and would prevent the Government from sustaining a default termination any time a contractor could craft a defense implicating state secrets, no matter how lacking in merit. This result does not impermissibly burden the contractors.

Moreover, the Government was not under an implied duty either to forfeit the Navy's right to terminate for default or to permit the disclosure of state secrets so as to enable the contractors to litigate their superior knowledge claim.

Finally, the contractors claim that the trial court should have sustained their affirmative defense of superior knowledge -- without trial, or even any evidence -- is without merit because it is based upon principles of criminal law that do not apply in a civil case.

At bottom, the contractors assumed the risk of their failure to perform the FSD contract that they had aggressively proposed in 1987. Among these risks were that the FSD contract could cost more to perform than the price the Navy would pay them, and that they would have to return all unliquidated progress payments if the contract were terminated for default. It is not a forfeiture to insist that the contractors fulfill the express terms of the contract into which they eagerly and freely entered. Indeed, these terms permit the contractors to keep forever $1.35 billion in liquidated progress payments, despite their default and despite never having delivered a single aircraft.

The judgment below should not be read as impairing the Government's ability to collect the monies it permitted the contractors to hold upon a temporary basis, and, to the extent the judgment is construed as compromising the Government's rights under the Deferment Agreement, that portion of the judgment should be reversed.

* * * *

E. The Trial Court Correctly Addressed The Defense of Superior Knowledge

After completion of the trial upon their default,

the contractors contended that the trial should have never taken place because the removal of their superior knowledge defense from the litigation allegedly required the court, as a matter of law, to hold that the Navy had forfeited its right to terminate the A-12 contract for default. *See* JA87,923-24; 87,727; 87,731; 88,662; 88,684-85; 88,689; 88,684-86. This contention is incorrect.

1. There Was No Duty To Share Classified Information

The contractors' contention relating to superior knowledge rests upon the incorrect premise that the Navy was under a duty to share classified information, including information contained in other "special access" and "unacknowledged" (*i.e.*, covert) programs operated by other agencies, including the Air Force's B-2 and F-117A aircraft programs among others.[23] GD Br. 49-51. No such duty existed.[24]

The A-12 contract *did* provide for the disclosure of specifically-identified information to the contractors, but, pointedly, *did not* provide for the disclosure of the classified information to which the contractors allege they were denied access. *See*

[23] They also contend that the Navy should have shared information contained in Northrop's competing bid for the A-12 contract, GD Br. 49-50, information which was protected by, among other proscriptions, 18 U.S.C. § 1905; 48 C.F.R. §§ 15.601, 15.610(d) (1985), at the time the contractors contend they required it -- prior to award. JA87,048.

[24] The brief of NDIA incorrectly assumes both that such a duty existed and that the Navy did not fulfill it.

JA25,524-56. Contrary to established law, the contractors contend that the existence of this express contract provision explicitly detailing the parties' agreement regarding information to be provided by the Government does not preclude application of the doctrine of superior knowledge regarding other information.

The doctrine of "superior knowledge" is a judicially developed doctrine which implies the assumption of a duty by a contracting agency to disclose to a contractor information in the agency's possession which, if disclosed, would prevent the contractor from embarking upon a "ruinous course of action." *Helene Curtis Indus., Inc. v. United States*, 312 F. 2d 774, 778 (Ct. Cl 1963). While an implied duty may exist with respect to the disclosure of some types of knowledge, the Navy bore no implied duty to disclose to the contractors voluminous amounts of detailed, highly classified information contained in "special access" programs operated by other agencies.

The contractors rely solely upon *J.A. Jones Constr. Co. v. United States*, 390 F.2d 886 (Ct. Cl. 1968), for the proposition that a duty of disclosure can be implied in the context of classified information. GD Br. 48; *see also McDonnell Douglas Corp. v. United States ("McDonnell V")*, 37 Fed. Cl. 270, 275, n.7 (1996). *J.A Jones* held that the superior knowledge doctrine can be invoked against the Government when the Government could have provided the contractor an unclassified "general warning," without the need to disclose classified information. 390 F.2d at 893 n.14 ("the evidence

falls far short of proving that a general warning to plaintiff would have rent the security blanket").

Here, no comparable unclassified general warning of the kind specified in *J.A. Jones* could have been given. Neither *J.A. Jones*, nor any other case, suggests that the Navy was obliged to warn two of the world's largest and most sophisticated defense contractors, *e.g.*, JA35,829, that the FSD contract to develop and build a new, carrier-based, stealth aircraft might be difficult to perform. *See American Ship Building Co. v. United States*, 654 F.2d 75, 79 (Ct. Cl. 1981) ("Perhaps plaintiff wished the government had prominently displayed in the invitation to bid a proviso that 'only knowledgeable and experienced contractors need apply.'").

Moreover, the contractors' claim extends far beyond a claim that they were entitled to a general warning to a claim that the Navy was under an implied duty to provide them with classified information. *J.A. Jones* does not remotely suggest that the Government has an obligation, under the superior knowledge doctrine, to disclose actual classified information. Indeed, to imply a contractual duty to disclose some of the Nation's most closely held national security secrets, as the contractors urge, would be contrary to both law and common sense. No court has ever found that the Government has a duty to disclose to its contractors classified information, particularly information contained in "special access" and "unacknowledged" programs operated by other agencies. These "special access" programs are subject to particularly strict

regulation. 32 C.F.R. §§ 159 *et seq.* (1988). The very purpose of classified, "special access" programs is to wall off the information in the program from other classified information and programs. JA434. Likewise, the purpose of "unacknowledged programs" is to limit knowledge that a program even exists to only those approved for access. *Id.* Both of these features operate as a damage control "brake" in the event of an unauthorized disclosure. *Id.* The strict security requirements governing classified information, JA432-33, and the Executive's constitutional and exclusive power to control access to that information, *Department of Navy v. Egan*, 484 U.S. 518, 527 (1988), would be undermined if a duty to disclose such information could be implied simply "from the circumstances of contracting." *See Hercules, Inc. v. United States*, 516 U.S. 417, 429 (1996); *see, e.g.*, Exec. Order No. 12958, 60 Fed. Reg. 19825; 18 U.S.C. § 793; 32 C.F.R. §§ 154 *et seq.*

In addition, the contractors' claim to classified information extends far beyond a claim for "some" classified information. Rather, they allege that the Navy had a duty to provide them with "[e]verything that the government knew for the low-observable program prior to award," which is contained in the classified, compartmented programs of all the military services. JA87,048; *see* GD. Br. 49 ("The Government, ... never provided *all of the critical information* it possessed.") (emphasis supplied); *id.* 50.[25]

[25] While acknowledging that they had received access to some information from the B-2 and F-117 programs, the contractors

The trial court initially accepted the contractors' contention that, pursuant to *J.A. Jones*, the contractors could attempt to demonstrate that the Navy failed to provide them with a "general warning" concerning an "impending avalanche" and permitted the contractors to conduct "limited discovery." *McDonnell Douglas v. United States* ("McDonnell II"), 27 Fed. Cl. 204, 206 (1992). Over the years, however, the court expanded the scope of discovery to permit the contractors to seek detailed classified information on "weight estimation techniques, application of low-observable technologies, propulsion systems technologies, composite materials and manufacturing technologies, and avionics technologies," 37 Fed. Cl. at 274, from other programs including the B-2 and F-117A programs. This discovery far exceeded the scope of *J.A Jones* or any recognized definition of the superior knowledge doctrine, and was contrary to this Court's holding that the contractors have no right to conduct a "wide-ranging fishing expedition" in the Government's classified world in an attempt to locate some evidence that might support a claim. *See Monarch Assurance P.L.C. v. United States*, 244 F.3d 1356, 1365 (Fed. Cir. 2001).

Even if, contrary to *J.A. Jones*, there were an implied duty to share actual classified information,

pointedly complained that "the information actually provided [was only] general in nature." JA65,559. The contractors took pains to emphasize that the "[o]verview and conceptual information" given to them was only "of minimal use" precisely because "*[t]he [supposedly] vital information necessary [was] at the detailed level.*" JA68,554 (emphasis supplied).

in the context of "special access," covert programs, the Navy cannot be constructively charged with possession of all knowledge contained in these programs, including programs operated by other agencies. *Bethlehem Corp v. United States*, 462 F.2d 1400, 1404 (Ct. Cl. 1972) ("Knowledge of a different Government agency is not to be attributed to the contracting agency.") (citations omitted); *S.T.G. Constr. Co., Inc. v. United States*, 157 Ct. Cl. 409, 416-17 (1962); *Bateson-Stolte, Inc. v. United States*, 172 F. Supp. 454, 457 (Ct. Cl. 1959). Morever, even the traditional superior knowledge doctrine does not require the Government to disclose all possible knowledge it may possess on a given subject. *Piasecki Aircraft Corp. v. United States*, 667 F.2d 50, 59 (Ct. Cl. 1981) ("mere governmental failure to disclose *each and every bit of information it has* clearly is not, in and of itself, enough to serve as a basis for contractor recovery.") (emphasis added); *Helene Curtis*, 312 F.2d at 779 n.2 (Government is not necessarily "required to disclose *all* of its information") (emphasis supplied); *American Ship Building*, 654 F.2d at 79 (Government not liable to disclose all difficulties and delays experienced by prior contractor on a similar project.)

In short, the Navy had no legal duty to disclose any classified information, let alone all information contained in all Government classified, "special access" and unacknowledged stealth programs and the contractors had no legal right or reasonable expectation that it would be provided to them.

2. The Contractors Do Not Have A "Valid" Superior Knowledge Defense

The trial court held that it "cannot know whether [the contractors' affirmative defense of superior knowledge] has merit." 50 Fed. Cl. at 325. Although they do not directly challenge this holding, the contractors, citing an earlier 1993 order, contend that the trial court "already held" that they had established a *prima facie* case of superior knowledge, GD Br. at 48, and insist that their superior knowledge defense was "plainly a substantial one, both legally and factually." GD Br. at 49. They thus hope to convey the impression (notwithstanding the trial court's explicit holding) that the trial court actually deprived them of a "meritorious" affirmative defense. GD Br. 27; *see generally id.* at 8, 11, 24, 48-51.

The contractors misrepresent the record. The contractors' claim lacked merit as a matter of law (as demonstrated above) and was also without merit as a matter of fact. Moreover, the trial court specifically rejected the contractors' claims that they had a "valid" defense.

Although the contractors do not challenge the trial court's holding that its superior knowledge claim cannot be litigated, GD Br. 50, GD nonetheless sets forth numerous factual allegations in its brief that supposedly support the contractors' superior knowledge defense. GD Br. 8, 48-50; MDC Br. 54. We were willing to establish facts below, 50 Fed. Cl. at 325, that would have defeated entirely any possible superior knowledge claim, including: (1) the

contractors' own claims, pre-award, of their prowess and experience with stealth technology, *see, e.g.*, 35,814; 68,580; 68,586; (2) the contractors' representations, pre-award, that they would subcontract with other companies, such as Lockheed (builder of the F-117A aircraft) to improve their stealth capabilities, JA68,580; 68,585; (3) the Navy's clear warning to the contractors, pre-award, that, in the Navy's view, the contractors' estimated weight of their design was too low by several thousand pounds, JA74,935; 21,195, 71,256; 70,681; (4) the contractors' self-confirmation, shortly after award, without any B-2 or F-117A information, that they had substantially underestimated their design's weight, JA71,256-57; 72,550-51; 70,509-10; and (5) the contractors' rejection of Navy efforts to grant them comprehensive access to the Air Force's B-2 and F-117A programs, JA87,498501.[26] We informed the

[26] Even though it is never legally bound to disclose classified information, the Executive Branch, of course, is vested with the discretion to afford access to classified information if it determines that to do so would be in the national interest. *See, generally, Egan*, 484 U.S. at 527. Here, and in the trial court below, the contractors acknowledge that the Government did, after award, afford them access to the B-2 and F-117A programs, but complain that the access was either untimely or not at a sufficiently detailed level. *See* GD Br. 49, 50; JA68,561-62. Any complaints by the contractors of inadequate access to these programs, if true, was a problem entirely of the contractors' own making. The Navy vigorously pushed the contractors to avail themselves of all information from certain Air Force programs, but the contractors, citing proprietary and business concerns, refused to cooperate in a more fulsome exchange of information with Air Force contractors, such as Northrop. JA87,498-501; *see Northrop Corp. v. McDonnell*

trial court that all of these facts could have been tried using unclassified or A-12 classified-only information. 50 Fed. Cl. at 325. *See, generally*, JA87,078-126.

In fact, the court indicated that the privileged material related to a Government *defense* to the contractors' claim that the Navy had failed to disclose superior knowledge. The court noted that the Government "might be unfairly prejudiced if discovery were restricted" to the B-2 and F-117A programs, 37 Fed.

Cl. at 281, and stated,

> [P]laintiffs' superior knowledge claim requires that the parties have access to information that the Air Force cannot impart for security reasons. We have established that it is not proper to consider plaintiffs' *prima facie* evidence in a vacuum when defendant might refute plaintiffs' evidence with greater access.

Id. at 282. *See id.* at 280 (". . . but defendant may be unfairly prejudiced if discovery were restricted to these programs [*e.g.*, B-2 and F-117A]"); *id.* at 281 ("if trial proceeded on this claim, ... defendant may be unable to defend itself."); *id.* at 284 ("The Government's defense relies heavily on classified information that would be extremely vulnerable if introduced").

Douglas Corp., 705 F.2d 1030 (9th Cir. 1983). *See generally*, *e.g.*, JA87,112-16; 87,450-52; 87,440-43.

In any event, the trial court held that it could not "know fully the effects that privileged information omitted from evidence would have for the parties in this case." *Id.* at 284. It concluded that, at some point, litigation of the superior knowledge claim would likely encounter material protected by a state secrets privilege. *Id.* at 277, 282-84. The identity of the party harmed by the invocation would depend upon the stage of the litigation at which the privilege was invoked. Thus, contrary to the contractors' contentions, the trial court did not hold that the invocation of the privilege deprived them of a valid defense. 50 Fed. Cl. at 325; *see also* JA455 ("The assertions made [by the contractors regarding their superior knowledge claims] cannot be established.")

3. The Trial Court Correctly Applied Well-Established Precedent In Dismissing The Superior Knowledge Claim

Once the trial court held that litigation of the superior knowledge claim would lead to an unacceptable risk of the disclosure of state secrets, it correctly followed bedrock precedent by removing the issue from the case and proceeding to litigate the remainder.

When presented with the invocation of the state secrets privilege, JA431-36,[27] the trial court properly

[27] The *classified* version of Air Force Secretary Peters' declaration, containing a more detailed explanation of the nature of the state secrets involved and the reason for the invocation (along with other related classified declarations, *see*

discharged its obligations to verify that the privilege was properly invoked. *See United States v. Reynolds*, 345 U.S. 1, 10-11 (1953); 37 Fed. Cl. at 278. After conducting this review, the trial court was fully satisfied that the invocation was valid. JA429-30; *see* 37 Fed. Cl. at 282-83.

Where, as here, there has been a valid invocation of the state secrets privilege, its effect is to remove the privileged information from the case. *Kasza v. Browner*, 133 F.3d 1159, 1166 (9th Cir. 1998); *Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1141 (5th Cir. 1992), *cert. denied*, 507 U.S. 1029 (1993); *In re United States*, 872 F.2d at 476. If the information is essential to an issue upon which a party bears the burden of proof, that issue will be decided against that party, based upon a failure of proof, if it is impossible to devise procedures which protect the privilege and yet allow merits to be decided. *DTM Research, L.LC. v. AT&T Corp.*, 245 F.3d 327, 334 (4th Cir. 2001) (court should attempt to "devise procedures which protect the privilege and yet allow the merits to be decided in some form" unless "any attempt to proceed will threaten disclosure of privileged matters").

Our burden below was to establish our claim of default. No information concerning other classified programs was necessary to present our claim that the contractors were in default. Thus, the removal of the state secrets from the case did not prevent us

37 Fed. Cl. at 281-283), is available to the Court for review by contacting the Air Force security official identified in the separate notice we are filing with this brief.

from proceeding and, as the trial court found, we met our burden. 50 Fed. Cl. at 325, 326.

The contractors bore the burden to prove their defenses, including the claim that the Navy failed to disclose superior knowledge. *See Lopez v. A.C. & S., Inc.*, 858 F. 2d 712, 717 (Fed. Cir. 1988) (contractor asserting superior knowledge claim must "produce specific information to support its contention"). Over the course of many years, the trial court attempted to devise a procedure which would enable the parties to litigate this claim without risking the disclosure of state secrets. After the court denied our motion to dismiss the superior knowledge claim in 1992, 27 Fed. Cl. at 204, the court permitted the contractors to conduct discovery into other classified programs. Discovery was halted in 1993, resumed again in 1994, and was finally halted in 1996 when the court decided that the risk of disclosure posed by further litigation of the issue was too great, a conclusion it reaffirmed after remand. The contractors do not challenge this ruling. GD Br. 47.

Under these circumstances, pursuant to *DTM Research*, *Kasza*, and *Bareford*, the trial court properly removed the issue from the case and proceeded to litigate the remainder.[28] The trial court

[28] The same principles apply to MDC's allegations regarding the contractors' requests for equitable adjustments ("REAs"). MDC Br. 54-55. These REAs have never been specified or quantified. Further, neither contractor presented any evidence in support of their REAs, which are based upon several legal theories, only one of which was the alleged withholding of "superior knowledge." Indeed, as the trial court noted, the contractors abandoned all efforts to litigate their impossibility and

made a substantial effort to litigate the contractors' claim. Upon determining that the invocation of the privilege was proper, 50 Fed. Cl. at 325, *see also* 37 Fed. Cl. at 283, the court concluded -- after attempting to do so -- that it could not devise procedures to adequately try the contractors' claims and simultaneously protect national security, 50 Fed. Cl. at 324. Thus, the trial court did everything that precedent required.

4. Invocation Of The State Secrets Privilege Did Not Forfeit The Right To Terminate For Default

The contractors contend that, regardless of the merit of their superior knowledge claim, by entering into the A-12 contract, the Navy agreed that if the Government ever invoked the state secrets privilege in such a manner as to make it impossible, as a practical matter, to litigate a defense to a termination for default, the Navy would forfeit its right to terminate the contract for default. *See* GD Br. 54-55; *see also* JA87,929-30; 87,732-33; 88,891; 88,926-28.

There is no provision in the contract which expressly contains the promise alleged by the contractors. In recognition of this fact, the contractors relied below upon the portion of the disputes clause which provides for "resolution of all

commercial impracticability claims. 50 Fed. Cl. at 325-26. Thus, having forfeited its opportunity at trial to establish its claims and defenses, MDC may not contend upon appeal that there remain significant outstanding REA issues to be decided before the default could be sustained.

disputes." JA88,926-28. According to the contractors, the Government's invocation of the state secrets privilege in a manner which prevents litigation of an issue constitutes a breach of the disputes clause, and thus prevents the Navy, as breaching party, from terminating the contract for default.

Clearly, the disputes clause says no such thing. Even if it could be twisted to mean that all disputes would be resolved, it could mean only that they would be resolved according to the established rules and principles applicable to the resolution process, including litigation, and that the application of these rules could adversely affect either party. As we have shown, the trial court's treatment of the superior knowledge issue here followed these principles.

Contrary to the claims of GD and NDIA, this result does not require the contractors to bear a burden which should be borne by the public as a whole. GD Br. 55; NDIA Br. 17-18. Unlike the takings cases upon which they rely *e.g.*, N DIA Br. 17, this case involves a consensual transaction between the Government and the contractors. The contractors were sophisticated businesses which had long participated voluntarily in the defense industry and in covert programs. As NDIA concedes, contracts in the defense industry carry a "significant potential" for invocation of the state secrets privilege. NDIA Br. 18. The contractors here knew that the Government might have to claim state secrets in the course of any dispute in

order to protect national security, and they knew that the legal principles applicable in that eventuality could affect them as well as the Government. Had the contractors wished to shift the entire risk of the assertion of a privilege to the Government, they should have negotiated for a clause broader than the clause to which they agreed, raised their prices to account for the risk, or, failing that, refused to enter into the contract.

To adopt the contractors' contention as the rule to be applied in the absence of an express provision, *see* GD Br. 54-55; NDIA Br. 2, 5, would establish a *per se* rule prohibiting a termination for default whenever a contractor's attorney is clever enough to craft a defense or argument implicating state secrets.[29] This outcome would violate the settled rule that the Government cannot be "punished for asserting the [state secrets] privilege." *Salisbury v. United States*, 690 F.2d 966, 975 (D.C. Cir 1982); see *also In re United States*, 872 F.2d 472, 476 (D.C. Cir.) *cert. dismissed*, 493 U.S. 960 (1989) ("Notions of sovereign immunity preclude any further adverse consequence to the government, such as alteration of procedural or substantive rules.").

5. Dismissal Of The Superior Knowledge Defense Did Not Violate Due Process

The contractors' "due process" contention makes

[29] *See* 50 Fed. Cl. at 325 (rejecting contractors' "new argument," raised after 11 years of litigation, that state secrets invocation somehow prevented them from establishing alleged impossibility defense).

liberal use of terms such as "prosecute" and "forfeiture," in a misdirected attempt to rely upon cases applying evidentiary principles that are applicable only the context of criminal law. *See, e.g., Washington v. Texas*, 388 U.S. 14 (1967); *Jencks v. United States*, 353 U.S. 657 (1957); *Roviaro v. United States*, 353 U.S. 53 (1957); *United States v. Andolschek*, 142 F.2d 503 (2d Cir. 1944). None of these cases directly concerns the state secrets privilege. Of them, only *Jencks* even addresses matters touching on national security.

The Supreme Court has recognized that the rationale underlying cases that address the consequences of excluding evidence from a criminal proceeding when the Government invokes certain privileges have no applicability in civil matters. In the seminal case of *Reynolds*, the Court explained the distinction:

> The rationale of the criminal cases [to the effect that the Government can invoke its evidentiary privilege only at the price of letting the defendant go free] is that, since the Government which prosecutes an accused also has the duty to see that justice is done, it is unconscionable to allow it to undertake prosecution and then invoke its governmental privileges to deprive the accused of anything which might be material to his defense. Such rationale has no application in a civil forum where the Government is not the

> moving party, but is the defendant only on terms to which it has consented.

345 U.S. at 12.

The other principal line of cases upon which the contractors and their *amicus* NDIA rely in support of their due process arguments address the general effect of asserting a privilege, other than the state secrets privilege. *See, e.g., Afron-Lecon, Inc. v. United States*, 820 F.2d 1198, 1205 (Fed. Cir. 1987); *Ideal Electronic Sec. Co. v. International Fidelity Ins. Co.*, 129 F.3d 143, 151 (D.C. Cir. 1997); *Lyons v. Johnson*, 415 F.2d 540, 542 (9th Cir. 1969). Those cases are cited for the general proposition that a privilege may not be used as both a sword and a shield by pressing a claim whose fair adjudication requires access to certain information while, at the same, time maintaining a privilege to withhold the information. *See* GD Br. 51-53; NDIA Br. 7-8.

This principle has no applicability here. We did not rely upon state secrets at trial to demonstrate the contractors' default. Our default evidence was drawn exclusively from the A-12 program, and, as previously discussed, the contractors had access during discovery to a broad range of classified documents or information, including any that we used. Nor, as NDIA erroneously suggests, did the contracting officer rely upon state secrets from outside the A-12 program in making his initial default determination. *See* NDIA Br. 11-12, 15 n.5. He terminated the contract because of the contractors' failure to make progress toward timely accomplishment of the contract's requirements.

JA1,515-17, 18,297.[30]

After eleven years of litigation, including five trials and two appeals on the merits, the contractors have been accorded all the procedural protections that the due process clause requires.

* * * *

[30] The other cases upon which the contractors and NDIA rely in support of their due process arguments are either cumulative of the cases discussed above, or even more remote in their relevance to the superior knowledge issues in this case.

IN THE UNITED STATES
COURT OF FEDERAL CLAIMS

No. 91-1204 C

MCDONNELL DOUGLAS CORPORATION
AND GENERAL DYNAMICS CORPORATION,

JUDGMENT

v.

THE UNITED STATES

Pursuant to the court's Published Order and Opinion, filed May 3, 2007, granting defendant's motion for judgment upon additional findings, and denying plaintiff's cross-motion and all pending motions,

IT IS ORDERED AND ADJUDGED this date, pursuant to Rule 58, that judgment is in favor of defendant. No costs.

Brian Bishop
Clerk of Court

May 3, 2007 By: s/Lisa DeFade Reyes
Deputy Clerk

NOTE: As to appeal, 60 days from this date, see RCFC 58.1, re number of copies and listing of *all plaintiffs*. Filing fee is $455.00.

PETITIONER'S BRIEF

FILED
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Nos. 09-1298 & 09-1302

IN THE
Supreme Court of the United States

GENERAL DYNAMICS CORPORATION,
Petitioner,
v.
UNITED STATES OF AMERICA,
Respondent.

THE BOEING COMPANY,
Petitioner,
v.
UNITED STATES OF AMERICA,
Respondent.

On Writ Of Certiorari To The
United States Court Of Appeals
For The Federal Circuit

BRIEF FOR PETITIONER GENERAL DYNAMICS CORPORATION

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November 12, 2010

385101

QUESTION PRESENTED

Whether the government can maintain its claim against a party when it invokes the state-secrets privilege to completely deny that party a defense to the claim.

LIST OF PARTIES AND CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 24.1(b) and Rule 29.6, the following list identifies all the parties to the proceeding before the United States Court of Appeals for the Federal Circuit:

General Dynamics Corporation, appellant below, has no parent corporation. No publicly held company owns ten percent or more of the stock of General Dynamics Corporation.

McDonnell Douglas Corporation, appellant below, was a wholly owned subsidiary of The Boeing Company prior to January 1, 2010. On that date, McDonnell Douglas Corporation merged into The Boeing Company, which is now the corporate successor of McDonnell Douglas Corporation. As of December 31, 2009, two companies disclose, in filings with the U.S. Securities and Exchange Commission, beneficial ownership of ten percent or more of the outstanding stock of The Boeing Company: State Street Corporation, a publicly held company whose subsidiary State Street Bank and Trust Company acts as trustee of The Boeing Company Employee Savings Plan Master Trust; and Evercore Trust Company, N.A., which acts as investment manager of The Boeing Company Employee Savings Plan Master Trust and which is a subsidiary of the publicly held Evercore Partners, Inc.

The United States.

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JURISDICTION

The Federal Circuit's judgment was issued on June 2, 2009. On November 24, 2009, the Federal Circuit denied petitioner's timely petition for panel rehearing or rehearing *en banc*. Chief Justice Roberts extended the time for filing a petition for certiorari to April 23, 2010, and the petition was filed that day. On September 28, 2010, this Court granted the petition in part and consolidated this case with *Boeing Co. v. United States*, No. 09-1302. This Court's jurisdiction rests on 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Fifth Amendment to the Constitution provides that "[n]o person shall . . . be deprived of life, liberty, or property, without due process of law." The following statutes and regulations are set out at Pet. App. 446a-72a: 41 U.S.C. § 605; 48 C.F.R. § 49.402-3; *id.* § 52.249-2; *id.* § 52.249-9.

STATEMENT OF THE CASE

The government terminated a multi-billion-dollar weapon system development contract with General Dynamics Corporation and McDonnell Douglas Corporation (together, the "Contractors") for default based on projected schedule delays – a forfeiture that exposed the Contractors to onerous penalties. That default would have become enforceable as a judgment if not timely put in issue. The Contractors therefore filed suit in the Court of Federal Claims, effectively vacating the default decision, requiring the government to prove its default claim *de novo* in court, and giving the Contractors their only opportunity to raise defenses. The Contractors' primary defense was that the government caused the delay that was the basis for the default by breaching its duty to share "superior knowledge" – that is, critical information unknown to the Contractors. The trial court found that the Contractors made a *prima facie* showing of a factual basis for this defense. But the government's assertion of the state-secrets privilege stripped the defense from the case, barring the Contractors from using even non-privileged evidence to raise it. The trial court recognized that the government had military secrets that needed protection, but expressed serious concern that the government was using secret information for its own purposes in the case and otherwise manipulating the judicial system to obtain a litigation advantage. Nevertheless, without any adjudication of the Contractors' primary defense, the trial court entered judgment for the government on its default claim. The Federal Circuit affirmed

because it gave dispositive weight to the fact that this is a civil case and the Contractors are nominal "plaintiffs."

A. Factual and Legal Background

In December 1986, the Navy sought proposals for full-scale design and production of a state-of-the-art weapon system called the "A-12 Avenger." Pet. App. 382a-83a & n.2; JA 349-50, 401. The A-12 was to be a stealth aircraft that would build on stealth technologies already in use in other government programs. Pet. App. 179a, 353a-54a.

As a premise of its acquisition strategy, the government planned to "shar[e] information" about these other programs, including the Air Force's B-2 aircraft program, with the A-12 contractors. *Id.* at 354a n.6; *see also* JA 646, 689; Pls' Mot. for Summ. J. at 8-9, Nov. 22, 1993 (Navy's Request for Proposals provided that contractors would make use of stealth technologies that were under development by the Air Force in the B-2 program). The Secretary of the Navy himself regarded it as an "unquestioned assumption . . . that [the Navy] would have full and unimpeded access to all of the B-2 technology," since that would save "an enormous amount of money" as well as "time and development process." Pet. App. 354a n.6. And the Deputy Assistant Secretary of Defense for Procurement, who initially opposed "putting the A-12 out for bids on a fixed-price contract[,] . . . relented only with assurance that the Government would share its stealth technology with the contractors. Otherwise, she predicted, it cannot be done." *Id.* at 64a n.16.

The Contractors were well aware of the government's plan to share information about stealth technology, which they had no other way of obtaining, and thus "had reason to expect that they would be granted . . . access." *Id.* at 353a-54a; *see also* JA 689. But the government did not grant access before submission of the Contractors' bid. JA 686-89.

A second bidder was Northrop Corporation, which built the B-2 bomber and therefore had extensive experience with stealth technology. Although it was not disclosed to the Contractors, Northrop's A-12 bid was $1.14 billion higher than the Contractors', for fewer aircraft, and its estimate of the weight of the aircraft was thousands of pounds heavier. *Id.* at 244-46, 1188-90; Pls.' Mot. for Summ. J. at 9, Nov. 22, 1993. Northrop also refused to bid on a fixed-price basis, as required by the Navy's solicitation, and capped its liability at $400 million. Pet. App. 384a n.3; JA 244-47.

The government knew Northrop's bid was probably "more realistic" because Northrop "had experience" that General Dynamics and McDonnell Douglas lacked. JA 45. But the government provided the Contractors neither relevant information nor a warning. Instead, in January 1988, it awarded the Contractors a fixed-price contract – on which they bore an unlimited risk of loss – to design, build, and test a series of increasingly sophisticated aircraft over a period of years.

To perform, "[t]he contractors wanted and needed highly sensitive technical information for the A-12, and the Navy wanted them to have it." Pet. App. 52a n.9. Indeed, the Navy promised that it would comply with its duty to share the relevant knowledge. JA 646-47, 658-62, 687, 689. But "the United States Air Force chose not to share its highly sensitive stealth information sufficiently to avoid technical difficulties and delay." Pet. App. 52a. The government ultimately did share a small amount of information, but it was too little and too late to be useful. JA 690-92.

As the Contractors learned lessons the government already knew, it became apparent that some of the "A-12 performance specifications were impossible to accomplish within the original time and cost projections." Pet. App. 355a. After extraordinary efforts, the Contractors informed the Navy that they could not meet the original weight specification or contract schedule. *Id.* at 55a-57a, 385a-87a. The Navy responded by accepting the Contractors' heavier design, *id.* at 57a, 388a-89a, and extending the schedule for delivery of the first eight aircraft, *id.* at 71a. The Contractors also sought financial relief, which the government denied. *Id.* at 95a-96a. Nonetheless, the Contractors informed the Navy they had made significant progress and remained committed to the A-12 program, and they continued to expend hundreds of millions of dollars every month to perform. *Id.* at 148a-49a & n.82.

Meanwhile, political support for the A-12 program was waning. With the Cold War over, the

military was reviewing its spending priorities, and the A-12 program fell victim to that review when then-Secretary of Defense Cheney decided to terminate it. *Id.* at 95a-97a, 395a n.9, 410a-11a. In so doing, Secretary Cheney "was not aware of the procedure or proper bases for terminating a contract" and "did not have a working knowledge of the contractors' . . . excuses for alleged non-performance," including the government's failure to share information about other stealth programs with the Contractors. *Id.* at 397a.

The Secretary's termination order came the day before the Navy was scheduled to obligate an additional $553 million in funds to the contract. *Id.* at 106a, 399a. The contracting officer and Navy counsel were therefore forced to cobble together a termination memorandum in haste. *Id.* at 397a-403a. They chose to terminate the contract for default on the theory that the Contractors had failed to "[p]rosecute the work" so as to make adequate progress, 48 C.F.R. § 52.249-9(a)(1)(ii) – even though the Contractors had not missed any unwaived deadlines, and even though the Navy had accepted the Contractors' design for the aircraft. Pet. App. 57a, 126a.

"Termination for default is a very serious sanction that rarely is applied by the Government." *Id.* at 229a n.11. In government-contract law, as reflected in the provisions of the A-12 contract, the government has the option of terminating for its convenience on a no-fault basis, in which case it is not liable for damages and need only reimburse the

contractor for costs reasonably incurred in performance to date. *See* 48 C.F.R. § 52.249-2. A termination for default, in contrast, is appropriate only if the contractor is in material breach of fundamental contract obligations. Such a termination imposes grave penalties on a contractor, amounting to a "forfeiture." Pet. App. 114a (quoting *DeVito v. United States*, 413 F.2d 1147, 1153 (Ct. Cl. 1969)). Not only does the government escape responsibility for paying the contractor's unreimbursed costs, but it also may seek return of payments it has previously advanced, as well as other monies, and may disadvantage or debar the contractor with respect to awards of future contracts. *See, e.g.*, 48 C.F.R. §§ 49.402-2(a), -6(c), -7(a); *Bannum, Inc. v. United States*, 91 Fed. Cl. 160, 171-72 (Fed. Cl. 2009).

In terminating for default here, the contracting officer performed no analysis of the Contractors' progress, performance, or reasons for any alleged non-performance, including the government's failure to disclose its knowledge about stealth technology. Pet. App. 410a-11a. Indeed, he "did not believe that the contractors would not perform." *Id.* at 167a; *see also id.* at 248a ("the Navy contracting officer did not want to terminate the contract"). Instead, he simply "cribbed" a prior termination memorandum from an unrelated program, leaving certain critical information blank. *Id.* at 411a. "The entire termination procedure was *pro forma* at best." *Id.* at 412a; *see also id.* at 98a-101a.

Following the default termination, the Navy sent the Contractors a letter demanding the payment of approximately $1.35 billion, plus interest. JA 339-41.

A default termination decision by the contracting officer becomes final and enforceable in a court of law unless the contractor files an action within certain statutory time limits. 41 U.S.C. § 605(b); *Seaboard Lumber Co. v. United States*, 903 F.2d 1560, 1562 & n.4 (Fed. Cir. 1990). Under the terms of the contract agreed to by both parties, such an action provides the mechanism for a contractor to defend against a default claim on the merits. 48 C.F.R. § 52.233-1 (Disputes clause). In the action, the contracting officer's decision has no force, and the government must start from scratch and prove *de novo* that the contractor was actually in default of its obligations under the contract. *See Lisbon Contractors, Inc. v. United States*, 828 F.2d 759, 764-65 (Fed. Cir. 1987); 41 U.S.C. §§ 605(a), 609(a)(3). If "it is determined that the Contractor was not in default, or that the default was excusable," the termination for default is converted to a termination for convenience. 48 C.F.R. § 52.249-9(g).

B. Procedural History

1. The Superior-Knowledge Defense Is Asserted.

To present their defenses to the default termination, the Contractors timely filed this action. Their primary defense was that the government failed to share its superior knowledge, *i.e.*, that they "were not in default of their A-12 . . . Contract

obligations by reason of the government's failure to disclose information vital to the Contractors' performance." JA 452. As relief, the Contractors sought a "judgment converting the termination for default to a termination for the convenience of the government" and a "holding that the Navy's demand for return of unliquidated progress payments is of no force and effect." *Id.* at 473.

The superior-knowledge doctrine is a contractual rule of fairness that prevents the government from knowingly allowing a contractor to pursue "a ruinous course of action." *Helene Curtis Indus., Inc. v. United States*, 312 F.2d 774, 778 (Ct. Cl. 1963). "It is well settled . . . that where the Government possesses special knowledge, not shared by the contractor, which is vital to the performance of the contract, the Government has an affirmative duty to disclose such knowledge." *Hardeman-Monier-Hutcherson v. United States*, 458 F.2d 1364, 1371-72 (Ct. Cl. 1972); *see* Pet. App. 270a ("This doctrine of superior knowledge is well established in law"). If the government holds its tongue, then it cannot complain of a resulting default.

Accordingly, when the government moved to dismiss the superior-knowledge defense on the ground that it had no duty to share its knowledge, the trial court denied the motion. JA 389, 393 (holding that "the Government had a duty to make *some* disclosure based upon its superior knowledge even though the basis for that knowledge was classified").

2. The State-Secrets Privilege Is First Invoked and the Trial Court Responds.

Shortly after discovery relating to the superior-knowledge issues began, the government filed a declaration by Acting Secretary of the Air Force Michael Donley formally invoking the state-secrets privilege as to certain classified information sought by the Contractors. JA 516-23. The state-secrets privilege is a common-law "privilege against revealing military secrets." *United States v. Reynolds*, 345 U.S. 1, 6 (1953). The privilege "belongs to the Government and must be asserted by it" through a "formal claim of privilege, lodged by the head of the department." *Id.* at 7-8. The court must then inquire whether, "from all the circumstances of the case, . . . there is a reasonable danger that compulsion of the evidence will expose military matters which, in the interest of national security, should not be divulged." *Id.* at 10; *see also id.* at 11 (noting that once the court determines the assertion of privilege is valid, "even the most compelling necessity cannot overcome the claim of privilege"). In the public version of Secretary Donley's declaration, he explained that "inadvertent, unauthorized disclosure of the information that is described in more detail in my *in camera* declaration could severely jeopardize national security" and that he could not even "confirm or deny the existence of the information" the Contractors sought. JA 521-22.

The trial court accepted the government's assertion of the privilege. However, after reviewing the government's *ex parte* submissions, the court

concluded that the government's litigation team had used the information as to which Secretary Donley had invoked the privilege "for tactical purposes involving the merits of plaintiffs' superior knowledge claim." *Id.* at 524; *see also id.* at 550 ("[S]ensitive information was used not only to argue Secretary Donley's invocation of the state secrets privilege but also for defendant's earlier litigation needs."). When the court sought "assurances from defendant that such use of sensitive information for tactical advantage will not recur," *id.* at 525, the government responded by "misrepresent[ing] the record," apparently hoping – in the court's estimation – to "rely on [the] problem of communication" caused by the need for secrecy to "misinterpret" the court's concerns, *id.* at 550-51. The court warned the government that its exploitation of the state-secrets power for tactical advantage "jeopardizes the [secret] information, gives [the government's] litigation team an unfair advantage," and "raise[s] serious implications under Rule 11." *Id.* at 551.

The parties disagreed about the effect of this first invocation of the privilege. The Contractors argued they could proceed on their superior-knowledge defense without the classified information the government had deemed secret, but the government argued this was not possible because the Contractors' "'superior knowledge' claims are inextricably intertwined with [protected] information." *Id.* at 586. The government added that it would be "a perversion to attempt to allow the judicial process to go forward" on superior-knowledge issues because the "informational poverty resulting

from invocation of the state secrets privilege . . . renders" those issues "nonjusticiable." *Id.* at 611.

Based on non-privileged evidence, the trial court ruled that the Contractors had "made an impressive showing that they can present a *prima facie* case [as to their superior-knowledge defense] under the existing discovery restrictions imposed by" the government, and therefore could continue discovery unless the government invoked the state-secrets privilege as to the entirety of the Contractors' superior-knowledge defense. *Id.* at 623, 625. In response, the government filed a declaration by Secretary of the Air Force Merrill McPeak. It stated that "continued inquiry into what is known as plaintiffs' 'superior knowledge' claims would necessarily require examination and use of information that cannot be disclosed in this litigation." *Id.* at 633. Secretary McPeak averred that "[l]itigation of plaintiffs' 'superior knowledge' claims would present a continuing threat of disclosure of information for which the military and state secrets privilege has been asserted, and would present a need for disclosure of additional information over which I would assert the privilege." *Id.*

The trial court then barred all discovery regarding superior-knowledge issues. *Id.* at 640-41. The court said it was clear that the Contractors "could establish a *prima facie* case" on the defense, and that "th[e] privileged information known to this court does not clearly establish that [the

government] could refute that showing." Pet. App. 441a. The court found, however, that it simply could not "resolve the merits" of the superior-knowledge dispute without "compromis[ing] military secrets." *Id.* The court also again expressed concerns about discovery abuses by the government. *See id.* at 432a-33a (discussing government violation of protective order concerning "access to certain classified information"); *id.* at 433a n.1 ("[d]uring the deposition of a government witness, [government] counsel deliberately elicited classified, compartmented information to further the government's case on the merits," a serious "security violation" that required "extraordinary corrective action" and "threatened the integrity of the litigation"); *id.* at 439a (discussing government's "security lapses").

As to the consequences of excluding superior knowledge from the case, the government argued that it should be allowed to pursue its default claim without litigation of the Contractors' "affirmative defense." JA 723-27. The court responded that although the "Government may choose not to cooperate [with discovery] because of legitimate concerns for national secrets, [it] must show the court why the cost of such a decision should be borne by plaintiffs" and "why we should not deem admitted" the Contractors' superior-knowledge allegations. *Id.* at 769.

Faced with losing its default claim, the government shifted position. Although it still maintained that no "portion of the 'superior

knowledge' claim . . . [was] truly separable from information subject to the state secrets privilege," upon "further reflection and consultation with senior Government officials" the government proposed a "framework for exploring whether further litigation of plaintiffs' 'superior knowledge' claims [was] possible." *Id.* at 773-75. Limited superior-knowledge discovery then resumed. *Id.* at 787-90.

3. The Trial Court Rejects Default on Other Grounds and Orders Reimbursement of the Contractors' Performance Costs.

Subsequently, the court ruled that the contract "was not terminated because of contractor default" but rather "because the Office of the Secretary of Defense withdrew support and funding from the A-12" for political reasons. *Id.* at 791. Having concluded that the default termination was pretextual and unjustified, the court again suspended superior-knowledge discovery, reasoning that it "may never become necessary" to litigate the defense. *Id.* at 795. After further trial proceedings, the court converted the default termination into a termination for convenience. Pet. App. 382a.

The superior-knowledge issue arose again, however, when the court held quantum proceedings to determine what, if anything, the Contractors were owed by the government in the termination-for-convenience context, where reimbursement of a contractor's incurred costs is standard. The Contractors had a claim for lost profits on work already performed based on the premise that the government breached its duty to share superior

knowledge; the government had a "loss ratio" argument for reducing reimbursement of incurred costs based on the premise that the government did not breach any duty and the Contractors would have lost money on the contract. Pet. App. 344a. Because both parties' arguments implicated information over which the government had already asserted the state-secrets privilege, the court decided to "spread[] the consequences of a difficult and dangerous problem." *Id.* at 381a. The court permitted the Contractors to recover their incurred costs (up to a contractual cap) with no adjustment of the contract price to reflect profit or loss. *Id.* at 380a-81a. Otherwise, the court concluded, it would necessarily be acting on "an incomplete record on which rulings . . . would be a sham." *Id.* at 379a-80a.

In so ruling, the court noted that "[u]nauthorized disclosures and questionable use of classification procedures by the Government have added to a general unease about litigating plaintiffs' equitable adjustment claims [based on the Government's superior knowledge] further." *Id.* at 376a. The court explained its concern that the government could strategically time its state-secrets-based objections to exploring certain topics to gain the maximum benefit. *Id.* at 369a-70a. It also reiterated its view that the government had made "misrepresentations" regarding its litigation use of secret information that it had withheld from the Contractors. *See, e.g.*, *id.* at 357a-58a & nn.9-10 (discussing why and how the government's "litigation team was given information so sensitive that the Air Force Secretary declared its disclosure for purposes of this litigation to be a

threat to national security," how the information was used, and what the government disclosed).

The court awarded the Contractors reimbursement of their actual costs (up to a contractual cap), in the amount of $1.2 billion plus interest. *Id.* at 342a; JA 884-85.

4. The Federal Circuit Reverses on the Default Issue.

On appeal, the government argued that it should have been permitted to press its loss ratio theory to avoid reimbursement of the Contractors' performance costs. At the same time, it argued that the Contractors' "superior knowledge and reasonable profits claims were properly removed from litigation because they jeopardized state secrets." Pet. App. 271a; *see also* JA 1234.

The Federal Circuit reversed on liability, holding that the termination was sufficiently "predicated on contract-related issues" that default could not be set aside solely on pretext grounds. Pet. App. 251a. It then remanded for an assessment of whether the default termination was actually justified on the facts. *Id.* Given the remand, the Federal Circuit vacated the trial court's rulings on superior-knowledge issues. It stated that due to the "passage of time and . . . possible intervening developments," it was in "no position to judge whether the risk of disclosure of state secrets [would] preclude adjudication" on remand, and the trial court was "free to reconsider this" in "the manner most fair and just to the parties." *Id.* at 271a.

5. The Privilege Is Invoked Again, and the Trial Court Upholds the Default While Barring the Superior-Knowledge Defense.

Hoping to find a way to litigate the whole case on remand, the trial court directed the parties to proceed with discovery on both the government's default claim and the Contractors' defense. JA 953-56.

The government then formally invoked the state-secrets privilege again. In an unclassified declaration of Secretary of the Air Force F. Whitten Peters (a classified, *ex parte* version was also filed), the government invoked the privilege over the "same matters that [had been] the subject of" earlier declarations. *Id.* at 975. Secretary Peters stated he had reviewed the 1993 declarations of Secretaries Donley and McPeak and determined that, even taking all possible precautions, there remained a "substantial risk that national security would be threatened" by disclosure of information concerning stealth aircraft. *Id.* at 975-76, 980.

The court then reaffirmed its earlier ruling that superior-knowledge issues had to be entirely removed from the case as they could not be litigated "safely." *Id.* at 985. The court explained that its determination was based on the classified version of Secretary Peters' declaration and the "warnings described therein" as well as the warnings contained in the earlier declarations, which the court found from "recent briefings" (to which the Contractors were not privy) still applied. *Id.*

The court invited the parties to address the effect of this ruling. *Id.* at 986. Reversing its earlier position, the government argued that the superior-knowledge issues could, after all, be tried safely using the limited discovery that had already taken place. *Id.* at 1013. If the court concluded that the superior-knowledge issues could not be tried safely, the government maintained that the Contractors' defense should simply be removed and the government permitted to press its default claim. *Id.* at 1051-53. And if it could not sustain its termination for default, the government argued that the "logical extension" of the court's state-secrets rulings "would simply be that both parties would walk away." *Id.* at 1216-17.

The court stood by its conclusion that "issues involving superior knowledge cannot be litigated safely." *Id.* at 1233-34. Indeed, the court noted that the government had previously represented to the Federal Circuit that the superior-knowledge issues were properly removed from the case because "they jeopardized state secrets." *Id.* at 1234.

The case thus went to trial on the propriety of the default with the Contractors' superior-knowledge defense removed from the case. The trial court ultimately ruled that the government had met its burden of proving default. Pet. App. 212a. The court relied solely on a finding that the Contractors would

not have been able to meet the "first flight" milestone date in the revised contract schedule. *Id.*[1]

6. The Federal Circuit Vacates But Allows the Government to Pursue Default While Using the Privilege to Bar the Contractors' Defense.

The Contractors appealed, arguing that the trial court misapplied the applicable default termination standards and denied the Contractors due process by allowing the government to pursue its default claim while barring the superior-knowledge defense. Pet. App. 182a, 207a. Reversing position yet again, the government contended that "[t]he trial court correctly addressed the defense of superior-knowledge." JA 1274; *see also id.* at 1273 (describing the trial court's "unchallenged holding"). The government also asserted that "the removal of the state secrets from the case" did not hamper the government's efforts to meet its burden to establish default. *Id.* at 1285-86. In the government's view, it was of no moment that the government's invocation of the privilege deprived the Contractors of a potentially dispositive defense. *Id.* at 1284-87, 1290-91.

[1] In addition, the court again explained that it could not definitively determine which party would have prevailed on the superior-knowledge defense. Pet. App. 245a ("We can never know enough to make a finding of fact on this issue."); *see also id.* at 246a. The court also adverted to a classified Appendix kept under seal at the Pentagon. *Id.* at 246a; *see also id.* at 345a & n.2.

The Federal Circuit vacated the trial court's liability ruling, directing the court to determine on remand whether the contracting officer could have had a reasonable belief that there was no reasonable likelihood of timely completion of the entire contract – not just the first contract milestone. Pet. App. 186a-87a. However, the Circuit affirmed the trial court's excision of the superior-knowledge defense from the case. *Id.* at 202a-10a. The court recognized that there is a "judicial aversion to default termination" because it is a "drastic sanction," acknowledged that the Contractors' superior-knowledge argument was a "defense" to that sanction, and agreed with the trial court that the defense could not be safely adjudicated. *Id.* at 190a, 202a, 207a, 209a. The court nevertheless concluded that the "Contractors [we]re not at jeopardy from an attack on them by the government," but rather were "the plaintiffs in this purely civil matter," *id.* at 208a, and therefore had to suffer the consequences when "a properly invoked claim of State Secrets privilege undercut[]" their "opportunity to prove [their] case," *id.* at 210a; *see also id.* at 208a-09a ("[T]he Fifth Amendment does not require that they be able to present all defenses, including a defense that would threaten national security.").

7. The Trial Court Rules Again for the Government and Is Upheld.

On remand, the trial court again addressed the merits of the default claim. The court concluded that there was no end date for contractual performance against which the Contractors' alleged "failure to

make progress" could be measured, *id.* at 122a, 127a, and acknowledged that default termination "is a forfeiture that is disfavored in the law," *id.* at 114a. Nevertheless, the court held the government had met its burden of proof by pointing to "reasons in retrospect why plaintiffs were not making the progress that some officials hoped and perhaps expected." *Id.* at 176a.

The Federal Circuit affirmed, undertaking a newly concocted "ad hoc, factual inquiry" into the "totality of the circumstances." *Id.* at 20a-21a. The decision did not comment further on the state-secrets issue.[2]

Following the Federal Circuit's decision, the government sent a letter to the Contractors demanding payment of $1,352,459,644 plus statutory interest from 1991. As of the date of the filing of this brief, the total government demand is $2,870,196,207.

[2] Although the Circuit had affirmed the removal of the superior-knowledge defense four years earlier, then-Chief Judge Michel – who had seen the case through three appeals and multiple mandamus petitions – expressed puzzlement at oral argument that the government failed to share the information needed by the Contractors: "[I]t looks to me as if had the Air Force [stealth] technology been handed over at the start of this contract to the two companies, . . . they would have met the dates, and the Navy would have got the plane it needed and wanted." Oral Arg. 1:12:44-1:13:02 (Fed. Cir. No. 2007-5111, Dec. 3, 2008), *available at* http://oralarguments.cafc.uscourts.gov/mp3/2007-5111Pt1.mp3.

SUMMARY OF ARGUMENT

The courts below adjudicated the government's default claim on the merits, even as the government's assertion of the state-secrets privilege prevented the Contractors from litigating their primary defense of superior knowledge. The Contractors made a persuasive showing (amounting to what the trial judge repeatedly found to be a *prima facie* case) that any schedule delay was a direct result of the government's failure to supply information about stealth technology before contract award and during contract performance. That defense, if proved, would have negated the government's claim of default. But although the trial court held that the defense was too intertwined with state secrets to be tried, it proceeded to adjudicate the default claim, entering judgment in the government's favor. That result was fundamentally unjust and a violation of due process.

1. In *United States v. Reynolds*, 345 U.S. 1 (1953), this Court recognized the importance of the state-secrets privilege as a means of protecting national security, and it instructed the lower courts to give great deference to the government when it formally invokes the privilege. At the same time, the Court recognized that it would be "unconscionable" to allow the government as the "moving party" to prosecute while using the state-secrets privilege to deprive the other party of a defense. *Id.* at 12. Since that time, the lower courts have applied a consistent approach in civil cases. Where the state-secrets privilege prevents a party from obtaining some

evidence potentially relevant to a defense, but does not effectively bar assertion of that defense, it operates like other evidentiary privileges, and the court proceeds to adjudicate the merits. Sometimes, however, the privilege does prevent a party from mounting a defense, either because the evidence withheld is so extensive and so central that the defense is effectively lost or because – as here – it is not possible to litigate an issue at all without risking national security. When a defense is barred, the rule is that the court may *not* proceed to adjudicate the claim. Instead, judgment must be entered for the party whose defense has been taken away.

That rule serves several critical purposes. First, it protects the basic fairness and integrity of the judicial process. If a court were to adjudicate the merits and impose liability on the non-moving party, even though a potentially dispositive defense could not be considered, it would have no way of knowing whether the outcome was legally and factually justified. Awarding affirmative relief under such circumstances would deny due process to the losing party. Moreover, it would risk the court's own legitimacy. When the just outcome is unknowable, a court must refrain from exercising its power in the claimant's favor, not take affirmative action that might very well be wrong.

The second basis for the rule comes into play when the moving party is the government itself, as in this case. Since the government is the sole party able to invoke the state-secrets privilege, and often does so with only minimal judicial oversight, the

privilege gives the government as litigant the ability to tilt the playing field in its favor. That reality, and the attendant risk of manipulation, may be unavoidable in cases where the government is defending against a claim. But when the government is the moving party with an affirmative claim, the risk becomes intolerable – and courts can and must take steps to assure that they do not become vehicles for imposition of liability on parties who are prevented from defending themselves because the government has said that their defense would risk national security. Courts do this not by second-guessing the government's assertion of the privilege, but by attempting to find ways to accommodate national security concerns while litigating the whole case and then, if that is impossible, by ruling in favor of the party that has been deprived of its ability to mount a defense. A private party should not be held liable or penalized, and the government permitted to reap a potential windfall, because of the need to protect state secrets for the benefit of the Nation as a whole.

2. In entering and affirming judgment for the government on its default claim, the courts below disregarded the principle that judgment must be entered in favor of a party that has been prevented from mounting its defense as a result of the state-secrets privilege. The Federal Circuit ruled for the government on the ground that this is a civil case and, as a formal matter, the Contractors are the "plaintiffs" in the caption. But a host of cases have recognized that civil parties may not be held liable after they have been deprived of a defense.

Moreover, the Contractors were "plaintiffs" here only in the most formalistic sense. A contractor, having received a default determination from a contracting officer, files suit in order to (1) trigger the government's burden of proving its default case and (2) allow the contractor to present defenses. In such a case, the government is in every meaningful sense the "moving party" on the default issue. *Reynolds*, 345 U.S. at 12. By using that term in *Reynolds*, the Court indicated that what matters in this area is substance, not empty formalisms.

The reality that the government is the moving party in a default case is driven home by the sanctions that may be imposed if there is a final determination that a contractor defaulted. The financial consequence may be a massive forfeiture of monies already paid for work actually performed. In addition, the contractor may be debarred from obtaining future contracts or may be handicapped in future bidding. Such potential consequences leave no room for doubt that the contractor is in the position of a defendant fending off the claim of the government as moving party. Indeed, those consequences are the reason why government contracts guarantee contractors the right to defend against a default in court, with the government bearing the burden of proof – a right that was effectively taken away here.

Entry of judgment for the government was also particularly inequitable here for two reasons. First, the record showed that the government abused its position by using privileged information to

strengthen its case even as it refused to produce such information to the Contractors. That kind of misuse of the privilege is foreclosed by the rule denying affirmative relief to the government against parties who are prevented by the privilege from mounting a defense.

Second, the superior-knowledge defense that the Contractors could not litigate was found by the trial court to be substantial and potentially dispositive. Legally, it is well established that the government owes its contractor assistance if it has knowledge superior to that of the contractor about the subject matter of a contract. Factually, the Contractors were able to submit sufficient evidence to make a *prima facie* showing on their superior-knowledge defense, even though they never received much of the evidence they sought in discovery. That showing established a strong basis for believing that the government caused the Contractors to fall behind because it forced them to reinvent complex stealth technology.

3. As a remedy, this Court should direct that judgment be entered for the Contractors on the default claim. In addition, the judgment of the trial court entered early in the case, when the termination had been converted to one for the government's convenience, should be reinstated. That judgment ensured that the default termination did not impose an unfair penalty on the Contractors because it reimbursed them for the costs they incurred prior to termination in performing the contract for the government's benefit. It also appropriately barred

both the government and the Contractors from arguing that the amount of actual costs should be adjusted (to reflect projected profit or projected loss), since both sides' arguments were intertwined with the superior-knowledge issue.

ARGUMENT

I. When the Government Is the Moving Party and Its Assertion of the State-Secrets Privilege Prevents the Defending Party from Presenting a Defense, the Court Must Enter Judgment for the Defending Party.

It was fundamentally unjust for the courts below to rule for the government on its default claim after the government's invocation of the state-secrets privilege prevented the Contractors from presenting their primary defense. In *United States v. Reynolds*, 345 U.S. 1 (1953), this Court recognized that it would be "unconscionable" for the government to prosecute a defendant after using the privilege to exclude evidence relevant to the defense. *Id.* at 12. That rule has been consistently followed in civil cases in which the invocation of the state-secrets privilege has had the effect of barring a party from asserting a potentially dispositive defense.

For several reasons, the rule is an essential corollary of the grant to the government of the unilateral power to assert the state-secrets privilege. National security does sometimes require limitations on the information the government may be forced to divulge, or restrictions on the issues that may be litigated. And because there is no alternative, the judicial system accepts that the government will

sometimes prevail as a defendant as a result of asserting the state-secrets privilege. But basic concerns about due process, judicial legitimacy, and the danger of unfair manipulation make it unacceptable to allow the government to use the privilege not just as a shield but also as a sword – to seek relief against a private party that has been prevented from defending itself by an assertion of the privilege. In that situation, the adversary process has ceased to function, and the government may not pursue its affirmative claim.

1. *Reynolds* was a civil suit in which private parties sued the United States, alleging that negligence caused the crash of a military airplane carrying civilians. The plaintiffs sought a classified report about the government's investigation of the crash, but the government objected that disclosure of the report would harm national security.

This Court held that "the privilege against revealing military secrets" was "well established." 345 U.S. at 6-7; *see also id.* at 7-8 n.18 (citing 1 Robertson's Reports 186 (Marshall, C.J.)). The Court upheld the assertion of the privilege as to the classified report, noting that such an assertion should often be accepted without any "examination of the evidence, even by the judge alone, in chambers." *Id.* at 10. But the Court nevertheless permitted the tort claim to proceed, since the privilege shielded only one particular document, and the plaintiffs

might have been able to prevail using other evidence. *See id.* at 11.[3]

The Court explained, however, that different rules apply where the government is pursuing its own claim. Thus, it would be "unconscionable" for the government – which "has the duty to see that justice is done" – to continue a criminal prosecution while "depriv[ing] the accused of anything which might be material to his defense." *Id.* at 12 (citing *United States v. Andolschek*, 142 F.2d 503, 506 (2d Cir. 1944) (L. Hand, J.)). The Court noted that this principle was inapplicable in the case before it, because the government was the defendant in a tort suit and could not in any way be considered "the moving party." *Id.* ("Such rationale has no application in a civil forum *where the Government is not the moving party, but is a defendant* only on terms to which it has consented" (emphasis added)). But where the government *is* the moving party, the Court suggested, a claim must yield if the state-secrets privilege makes an adversary adjudication

[3] The Court had previously addressed a related question in *Totten v. United States*, 92 U.S. 105 (1875), a suit to enforce an alleged secret contract between the government and a private citizen. The Court held that the entire suit was barred, explaining that "public policy forbids the maintenance of any suit in a court of justice, the trial of which would inevitably lead to the disclosure of matters which the law itself regards as confidential." *Id.* at 107.

impossible by preventing consideration of a potentially valid defense. *See id.*[4]

2. That result is required – in civil cases as well as criminal ones – by principles of justice that are fundamental to the operation of the courts. It is basic to our system of ordered liberty that a party is entitled to "an adequate opportunity to defend against the imposition of liability." *Nelson v. Adams USA, Inc.*, 529 U.S. 460, 466 (2000); *see also, e.g.*, *Lindsey v. Normet*, 405 U.S. 56, 66 (1972) (requiring "an opportunity to present every available defense" (internal quotation marks omitted)); *Am. Surety Co. v. Baldwin*, 287 U.S. 156, 168 (1932); *Saunders v. Shaw*, 244 U.S. 317, 319-20 (1917). That right has long been recognized to be among "those fundamental requirements of fairness which are the essence of due process in a proceeding of a judicial nature." *Morgan v. United States*, 304 U.S. 1, 19 (1938); *cf. Roviaro v. United States*, 353 U.S. 53, 60-61 (1957) (citing "fundamental requirements of fairness" in criminal case involving the consequences of the government's assertion of its privilege to withhold an informant's identity).

The issue is not just fairness to a particular litigant. There is also the need to protect the

[4] Notably, in its brief in *Reynolds*, the government argued that when it *is* the moving party and the state-secrets privilege prevents disclosure, "the Government is denied judicial assistance; but the public is left in no worse position than if it had never instituted the action." Br. of United States 17, *United States v. Reynolds*, 345 U.S. 1 (1953) (No. 21), *available at* 1952 WL 82378.

integrity and legitimacy of the judicial system. Neither the parties nor the public at large can have confidence in a judgment awarding affirmative relief in a case in which the state-secrets privilege has barred a defense that could change the result. As Justice Scalia once put it, if a party is "prevented from establishing a valid defense" and the court enters judgment, that "causes the courts of law not merely to let stand a wrong, but to become themselves the instruments of wrong." *Jaffee v. Redmond*, 518 U.S. 1, 19 (1996) (Scalia, J., dissenting); *cf. Poe v. Ullman*, 367 U.S. 497, 505 (1961) (stating that "[t]he Court has found unfit for adjudication any cause that is not in any real sense adversary," since that is "a safeguard essential to the integrity of the judicial process" (internal quotation marks omitted)); *Legal Servs. Corp. v. Velazquez*, 531 U.S. 533, 545-46, 548 (2001) (observing that blocking certain arguments "threatens severe impairment of the judicial function"). And that is no less true where the reason for the distortion in the process is the government's assertion of national security interests. *See, e.g., Kennedy v. Mendoza-Martinez*, 372 U.S. 144, 164-65 (1963).

Moreover, where – as here – the moving party is the government, there is an additional justification for a rule against imposing liability on the party deprived of a defense by the invocation of the state-secrets privilege. *See Reynolds*, 345 U.S. at 12. Because a court's ability to inquire into the reasons for asserting the privilege is limited, *see id.* at 10-11, the temptations of strategic misuse of the privilege to obtain affirmative relief are high, and the courts

must guard against such misuse. *See, e.g.*, Beth George, *An Administrative Law Approach to Reforming the State Secrets Privilege*, 84 N.Y.U. L. Rev. 1691, 1707 (2009); Br. of United States 63-64, *United States v. Reynolds*, 345 U.S. 1 (1953) (No. 21), *available at* 1952 WL 82378 (arguing that the agency head deciding whether to assert the privilege will necessarily be cognizant of effects on the government's position and the public fisc); Scott Armstrong, *Do You Want to Know a Secret*, Wash. Post, Feb. 16, 1997, at C01 (quoting government attorney saying that the government can "always play the trump card – state secrets – and close down the game").

One form of government misuse is assertion of the privilege without justification to obtain a litigation advantage. For instance, when the accident report at issue in *Reynolds* was declassified and released decades later, it turned out to contain no information about secret equipment – although it did decry the government negligence that caused the plane crash. *See, e.g.*, Meredith Fuchs, *Judging Secrets: The Role Courts Should Play in Preventing Unnecessary Secrecy*, 58 Admin. L. Rev. 131, 168 (2006); Barry Siegel, *Claim of Privilege* 210-11 (2008).[5] Another form of government misuse is

[5] The government has recently issued new guidelines for invoking the state-secrets privilege, but they do not lessen this concern, since there is no means of enforcing them. *See* Office of the Attorney General, *Policies and Procedures Governing Invocation of the State Secrets Privilege* at 4, Sept. 23, 2009, http://www.justice.gov/opa/documents/state-secret-privileges.pdf.

reliance on secret evidence – to which the other party never has access – to provide information, guide strategy, and otherwise advance the government's own affirmative case. The latter type of misconduct became a major concern of the trial court in this case, as the government developed its case using secret information while using a series of invocations of the privilege to withhold the information from the Contractors. *See supra* pp. 11, 13-16; *infra* pp. 53-54.

By contrast, there is little danger of strategic misuse of the privilege by private civil litigants seeking to defeat government claims by asking for disclosure of classified material. The government can often provide some but not all of the information requested. The court can determine whether the private party's discovery demands are overbroad or strategic, taking into account the information that the government is willing to share. Moreover, there are often ways to litigate issues while preserving some degree of confidentiality. *See, e.g., United States v. Zettl*, 835 F.2d 1059, 1063 (4th Cir. 1987); *see also infra* p. 51. Hence, only in exceptional cases will private parties be deprived of a potentially valid defense as a result of an assertion of the state-secrets privilege. When that occurs, however, the proper outcome is clear: judgment must be entered for the private party on whom the government is seeking to impose liability.

3. With the exception of the court below, the courts of appeals agree on that result, and have reached a consensus on how to determine whether a party has been "depriv[ed]" of a defense within the

meaning of *Reynolds*.[6] As with other privileges, invocation of the state-secrets privilege merely to remove *some* evidence from the case may have an impact on the truth-finding function of courts, but usually will not fundamentally impair the adjudicatory process. Thus, in many civil actions, invocation of the state-secrets privilege has the same effect as invocation of any other privilege: it merely removes some circumscribed subset of evidence from the case, which can thereafter continue to be adjudicated using ordinary procedures. *Mohamed v.*

[6] Since *Reynolds*, this Court has held that courts may not entertain lawsuits seeking to enforce secret contracts relating to espionage work for the government, *Tenet v. Doe*, 544 U.S. 1 (2005), but has not otherwise addressed the effect of protecting state secrets in civil cases. In the criminal context, the Court held subsequent to *Reynolds* that dismissal of a criminal prosecution is required when the government invokes the state-secrets privilege to withhold evidence that is relevant and material to the defense. *See Jencks v. United States*, 353 U.S. 657, 670-72 (1957) ("[t]he burden is the Government's . . . to decide whether the public prejudice of allowing the crime to go unpunished is greater than that attendant upon the possible disclosure of state secrets"); *cf. Roviaro*, 353 U.S. at 60-61. Congress then passed the Classified Information Procedures Act ("CIPA") to govern these issues in criminal cases. *See* 18 U.S.C.A. app. 3 § 4; *cf.* Mil. R. Evid. 505(e)(3). CIPA provides that where the government withholds on national security grounds information needed to ensure a fair trial, "the court shall dismiss the indictment or information." 18 U.S.C.A. app. 3 § 6(e); *see also, e.g.*, H.R. Rep. No. 96-831, pt. 2, at 3 (1980); *United States v. Fernandez*, 913 F.2d 148, 163-64 (4th Cir. 1990).

Jeppesen Dataplan, Inc., 614 F.3d 1070, 1082-83 (9th Cir. 2010) (en banc) (collecting cases).[7]

But the impact of the state-secrets privilege can be much more far-reaching, sometimes altogether preventing litigation of central issues. For example, as in this case, sometimes the relevant non-privileged evidence with regard to a given issue is so intertwined with state secrets that any litigation of the issue would present an intolerable risk. *See, e.g.*, *Fitzgerald v. Penthouse Int'l Ltd.*, 776 F.2d 1236, 1243 (4th Cir. 1985) (explaining that "state secrets could be compromised" during exploration of non-secret evidence, since "the parties would have every incentive to probe dangerously close to the state secrets themselves"). In such cases, the state-secrets privilege no longer resembles other privileges. Rather, as Judge Phillips recognized in an oft-cited opinion, "the undisclosable scope of privilege lies so completely athwart the scope of proof relevant to resolution of the issues presented that litigation constrained by administration of the privilege simply could not afford the essential fairness of opportunity to both parties that is a fundamental assumption of the adversary system." *Farnsworth Cannon, Inc. v. Grimes*, 635 F.2d 268, 279 (4th Cir.) (Phillips, J., dissenting from panel opinion), *panel op. vacated on rehearing en banc*, 635 F.2d 281 (4th Cir. 1980). In

[7] CIPA recognizes that where the privilege has a limited effect on a criminal defendant's defense the court may take action other than dismissal as "appropriate," such as finding against the United States on particular issues. *See id.* at 1082-83; *see also, e.g.*, H.R. Rep. 96-831, pt. 1, at 21.

this respect, the states secret privilege is "sui generis." *Id.* at 276.[8]

In these circumstances, a court must deny the affirmative relief sought by the moving party "not only when his claim but also when the defendant's defense is precluded by the privilege." *Id.* at 278. Thus, even if the moving party could establish the elements of its claim without using privileged material, a court cannot grant relief if the privilege altogether deprives the other party of its ability to prove a defense. Where the adversary process is so fundamentally impaired, imposing liability or a penalty on the defendant, or allowing the matter to go to trial without an opportunity for the defendant to put on its defense, would amount to a "mockery of justice." *Molerio v. FBI*, 749 F.2d 815, 825 (D.C. Cir. 1984) (Scalia, J.).

This rule applies in several different situations in which the state-secrets privilege effectively prevents a defendant from putting on a defense. In some cases involving less complex fact patterns, the information that a court reviews *in camera* to

[8] Indeed, in its first state-secrets decision, this Court recognized that a claim for relief may not proceed if its subject matter involves a state secret. *Totten*, 92 U.S. at 106-07. The same result follows when the evidentiary privilege against disclosure of state secrets results in a fundamental impairment of the adversary process. *See Jeppesen*, 614 F.3d at 1083 ("In some instances, however, application of the privilege may require dismissal of the action. When this point is reached, the *Reynolds* privilege converges with the *Totten* bar"); *cf. Weinberger v. Catholic Action of Hawaii*, 454 U.S. 139, 146-47 (1981).

determine the adequacy of the claim of privilege may also conclusively establish the defense to liability. *E.g.*, *id.* But even where a court cannot conclusively determine that the defense would succeed, it cannot rule for the claimant where the effect of the privilege is that the other party "cannot fairly present a good faith, colorable affirmative defense, or fairly rebut the plaintiff's prima facie case." *Farnsworth Cannon*, 635 F.2d at 280 (opinion of Phillips, J.). Likewise, courts have recognized that liability may not be imposed when the privilege *altogether prevents* litigation of the entire case or a key element of it, such as a complete defense to liability. *See, e.g.*, *id.* (liability may not be imposed where "the privilege so far obstructs normal proof in respect of the issues presented by the parties as to deprive the litigation process of its essential utility for fair resolution of those issues" or where "the danger of inadvertent compromise of the protected state secrets outweighs the public and private interests in attempting formally to resolve the dispute while honoring the privilege"); *Jeppesen*, 614 F.3d at 1083 ("even if the claims and defenses might theoretically be established without relying on privileged evidence, it may be impossible to proceed with the litigation because – privileged evidence being inseparable from nonprivileged information that will be necessary to the claims or defenses – litigating the case to a judgment on the merits would present an unacceptable risk of disclosing state secrets").

The courts of appeals have uniformly adhered to these principles, except in the decision under review. *See, e.g.*, *El-Masri v. United States*, 479 F.3d 296,

309-10 (4th Cir. 2007) (because "the defendants could not properly defend themselves without using privileged evidence," the claim could not go forward); *Tenenbaum v. Simonini*, 372 F.3d 776, 777 (6th Cir. 2004) ("We further conclude that Defendants cannot defend their conduct with respect to Tenenbaum without revealing the privileged information. Because the state secrets doctrine thus deprives Defendants of a valid defense to the Tenenbaums' claims, we find that the district court properly dismissed the claims."); *Kasza v. Browner*, 133 F.3d 1159, 1166 (9th Cir. 1998) ("[I]f the privilege deprives the defendant of information that would otherwise give the defendant a valid defense to the claim, then the court may grant summary judgment to the defendant" (quoting *Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1141 (5th Cir. 1992) (internal quotation marks omitted)).

Moreover, the government has consistently advocated that the United States, its employees, and its contractors may not be subjected to civil liability when they are sued by a plaintiff who can establish a *prima facie* case without privileged evidence, but a core defense cannot be litigated because of state secrets. The government has urged that "dismissal is required . . . if the [state-secrets] privilege claim . . . precludes the defendant" from asserting a defense, or "if the case is so suffused with privileged material that further proceedings would pose an undue risk of disclosing secret information." Br. of United States 13-14, *Mohamed v. Jeppesen Dataplan, Inc.*, 614 F.3d 1070 (9th Cir. 2010) (No. 08-15693) (en banc), *available at* 2009 WL 6635974; *see*

also, e.g., Br. of United States 35, *El-Masri v. United States*, 479 F.3d 296 (4th Cir. 2007) (No. 06-1667), *available at* 2006 WL 2726281 ("If the unavailability of the information protected by the privilege precludes either the plaintiff or defendant from establishing their respective legal positions on the issues in the case, then the case must be dismissed."); Br. of United States 35-36, *Sterling v. Tenet*, 416 F.3d 338 (4th Cir. 2005) (No. 04-1495), *available at* 2005 WL 871009 (requesting dismissal where "the Agency would be unable to present a defense" because of information protected by the privilege); *supra* note 4.

Indeed, the government has argued in support of that rule *in this very case*. When at an early stage the trial court addressed the Contractors' termination-for-convenience recovery, the court ruled that the government's invocation of the state-secrets privilege barred it from asserting a "loss ratio" argument that the government said would have reduced the recovery to zero. The government protested that it "was . . . grossly unfair to award plaintiffs their total costs when the Government was *deprived of a defense* which would have adjusted the amount of those costs as required by the contract and the Federal Acquisition Regulation." JA 1058-59 (emphasis added) (citing *Molerio v. FBI*, 749 F.2d 815 (D.C. Cir. 1984)); *see also id.* at 1025 n.2; *id.* at 746 n.7 (arguing for dismissal of claims on ground that "the Government is precluded from asserting its defenses . . . because those defenses . . . are inextricably intertwined with privileged matters").

II. The Contractors Are Entitled to Judgment in Their Favor on the Government's Claim of Default.

The application of the above-stated principles to this case is straightforward. The government's invocation of the state-secrets privilege altogether prevented the Contractors from presenting their superior-knowledge defense to liability, even though the trial court recognized the Contractors had shown a substantial basis for the defense on the merits. Under those circumstances, entering judgment for the government was a "mockery of justice." *Molerio*, 749 F.2d at 825. The Federal Circuit's contrary ruling rested on the fact that this is a civil case and the Contractors are the nominal plaintiffs. *See* Pet. App. 208a-10a. But there is no basis for limiting to criminal cases the rule that the government, as moving party, may not be awarded judgment if the privilege prevents the other party from offering a defense. Nor is there any doubt that the government is the moving party with regard to its default claim.

A. The Fact That This Is a Civil Case Does Not Justify Affirmative Relief for the Government.

The court of appeals found it significant that this is a "purely civil matter," suggesting that constitutional concerns raised when a criminal defendant is barred by the privilege from defending himself do not apply to a civil action. Pet. App. 208a-09a. But as the authorities cited in Part I demonstrate, such a distinction ignores decades of case law. It also makes no sense.

When the government is the moving party in a civil case, due process and judicial integrity bar the imposition of liability on a party deprived of a defense, just as in a criminal case. Moreover, as this case and *Reynolds* both illustrate, concerns about governmental manipulation of the privilege are no less salient in the civil context. It would be indefensible to adopt the Federal Circuit's apparent view that in civil cases there is no problem raised by awarding affirmative relief to the government after the losing party has been prevented by the government's invocation of the privilege from offering a defense.

B. The Government Was the Moving Party on Default.

Nothing in *Reynolds* or related cases supports the Federal Circuit's formalistic approach, under which the question of who is the "moving party" turns on the form of the case caption. Indeed, it is notable that *Reynolds* uses the term "moving party," rather than "plaintiff," in this context. 345 U.S. at 12.

1. The procedures chosen by the government for resolving default claims dramatically demonstrate why the Federal Circuit's simplistic approach is erroneous. It is hornbook government-contract law that a claim for default termination is a *government* claim, not a contractor claim. *See, e.g., Malone v. United States*, 849 F.2d 1441, 1443 (Fed. Cir. 1988) ("a government decision to terminate a contractor for default is a government claim"); 41 U.S.C. § 605(a) (provision of Contract Disputes Act distinguishing between "claims by the government" and "claims by

the contractor"); 48 C.F.R. § 2.101(a) (defining "claim" as an "assertion" that "seek[s], as a matter of right, . . . relief arising under or relating to the contract"). The government conceded this key point in its brief opposing certiorari. *See* Cert. Opp. 14-15 (citing *Malone*).

Although a default termination is a government claim, the law requires the *contractor* to bring suit in order to mount a defense against that claim. Specifically, when the contracting officer issues a decision terminating a contractor for default, the government's claim is set in motion. If the contractor does not timely defend itself against that decision – which normally includes, as in this case, a demand by the government for money, *see* JA 339-41 – then "the merits of that decision cannot be judicially challenged." *Seaboard Lumber*, 903 F.2d at 1562. Thus, "once the decision of the contracting officer becomes final," it has "preclusive effect" and can be automatically converted into a judgment enforceable against the contractor without any further inquiry into the merits of the government's claim or opportunity for the contractor to present valid defenses. *Id.*; *see also id.* at 1562 n.4 (explaining that "[t]he government may obtain a judgment on the basis of [a decision that becomes final in this manner] in a state or federal court without litigating the merits," and citing cases); 41 U.S.C. § 605(b) ("The contracting officer's decision on the claim shall be final and conclusive and not subject to review by any forum, tribunal, or Government agency, unless an appeal or suit is timely commenced as authorized

by this chapter."); *Renda Marine, Inc. v. United States*, 509 F.3d 1372, 1380-81 (Fed. Cir. 2007).

The contractor can interpose its defenses against the government claim only by filing an action under the Contract Disputes Act. Once a contractor files suit, the contracting officer decision is effectively vacated. The court addresses the default issue *de novo* with the government carrying the burden of proof, and the contractor can defend itself against the government's charge. *See, e.g.*, *Lisbon*, 828 F.2d at 764-65 (noting "long-established government contract law" that "the government bears the burden of proof on the issue of the correctness of its actions in terminating a contractor for default," which never "shifts . . . back and forth," and that "the government is only being made to bear the burden of proof of its own 'claim' of default"); 41 U.S.C. §§ 605(a), 609(a)(3) (stating that findings of fact by the contracting officer "shall not be binding in any subsequent proceeding" and that the action "shall proceed de novo"); *Assurance Co. v. United States*, 813 F.2d 1202, 1206 (Fed. Cir. 1987) ("the contracting officer's award is not to be treated as if it were the unappealed determination of a lower tribunal"); Pet. App. 269a (the contracting officer "meant not to take away the right of Contractors to assert their defenses to termination for default, he instead only meant to assert the government's right to allege material breach").[9]

[9] Indeed, one of the government's primary arguments has been that "unlike the court in an Administrative Procedure Act suit . . . the [court] in a [Contract Disputes Act] action does not

In short, there cannot be any doubt that the government was the moving party here. *See, e.g.*, *Wehling v. Columbia Broad. Sys.*, 608 F.2d 1084, 1089 n.10 (5th Cir. 1979) (noting that when a party "'voluntarily' becomes a plaintiff only because there is no other means of protecting legal rights," the plaintiff-defendant distinction is only "superficially appealing"). Confirming this reality, the government in the courts below repeatedly acknowledged the Contractors' superior-knowledge argument as an "affirmative defense" to the government's own claim. *See, e.g.*, JA 723-25, 762, 923, 1052, 1274.

2. The government's status as the "moving party" is driven home by the harsh consequences the Contractors could suffer if default liability is imposed. Default termination is a "species of forfeiture." *DeVito v. United States*, 413 F.2d 1147, 1153 (Ct. Cl. 1969). It has also been termed a "drastic sanction," *J.D. Hedin Constr. Co. v. United States*, 408 F.2d 424, 431 (Ct. Cl. 1969), and the "harshest punishment" the government can visit on a contractor, *Int'l Verbatim Reporters, Inc. v. United States*, 9 Cl. Ct. 710, 717 (1986); *see also H.N. Bailey & Assocs. v. United States*, 449 F.2d 387, 391 (Ct. Cl. 1971) (noting that a default termination is a "drastic sanction" and that the government must be "held . . .

review an administrative record," so that the government is "entitled to establish that a default termination is justified based on any grounds available, regardless whether those grounds were known at the time of termination." Cert. Opp. 27-28; *see also* Pet. App. 29a (Federal Circuit's endorsement of this principle).

to strict accountability for its actions in enforcing this sanction" (internal quotation marks omitted)).

A default termination carries monetary consequences, *see, e.g.,* 48 C.F.R. §§ 49.402-2(a), -6(c), -7(a), which can be draconian – as in this case, in which the government seeks a staggering sum. It also carries a variety of serious prospective penalties. It can prevent a contractor from being awarded future contracts, by branding the contractor not "responsible." *Bannum, Inc. v. United States*, 91 Fed. Cl. 160, 171-72 (2009) (holding that agency was "legally required" to consider prior default termination in subsequent contract award); 48 C.F.R. § 9.103(a); *see also id.* §§ 9.104-1(c), 9.104-3(b), 9.105-1, 42.1501; John Cibinic, Jr. & Ralph C. Nash, Jr., *Formation of Government Contracts* 416-20 (3d ed. 1998). Moreover, it may result in debarment of a contractor from *any* dealings with the government. *See Malone*, 849 F.2d at 1445.

3. Given the procedural scheme the government has created, and the crushing penalties the Contractors may face if the government prevails on its claim of default, it would violate the principles of fundamental fairness and due process on which the *Reynolds* rule is based to treat the Contractors as the moving party for purposes of that rule. The Contractors entered into the A-12 contract in reliance on contractual provisions incorporating the statutory and regulatory dispute resolution procedures assuring them the opportunity to require the government to prove any default claim, subject to their defenses. *See* 48 C.F.R. § 52.233-1 (Disputes

clause of the contract, which refers to relevant provisions of the Contract Disputes Act).

The decision below, however, deprived the Contractors of the process to which they – and the government – agreed. It allowed the government to obtain judgment on its default claim free of the Contractors' main defense. Even worse, it was the government that controlled whether the Contractors were able to litigate their defense, a power that in this case the trial court found had been abused for the sake of obtaining a litigation advantage. *See supra* pp. 11, 13, 15-16. No one would doubt that it would violate due process simply to leave in place the contracting officer's default decision – with all of its extraordinary consequences – without giving the Contractors a fair ability to challenge it. But that is functionally equivalent to what happened here. In the face of a default termination that otherwise would have become final and enforceable, the Contractors' suit was the only means they had to put their superior-knowledge defense before a neutral arbiter. *See Concrete Pipe & Prods. of Cal., Inc. v. Constr. Laborers Pension Trust*, 508 U.S. 602, 617, 626 (1993) ("due process requires a neutral and detached judge in the first instance" (internal quotation marks omitted)).[10] That opportunity was taken away from them, through no fault of their own.

[10] *See also, e.g.*, 41 U.S.C. § 601 revision note (explaining that the Contract Disputes Act was designed to "insure fair and equitable treatment to contractors and Government agencies"); 41 U.S.C. § 605 revision note (explaining that the contracting officer does not have to engage in any particular adjudicatory

Moreover, in the circumstances here, the government is best equipped to bear the consequences of the uncertainty created by its own assertion of the state-secrets privilege. This Court has long recognized that the United States should not "forc[e] some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole." *Dolan v. City of Tigard*, 512 U.S. 374, 384 (1994) (quoting *Armstrong v. United States*, 364 U.S. 40, 49 (1960)) (internal quotation marks omitted). The state-secrets privilege protects the Nation, and where the government is the claimant, costs associated with the privilege should be borne by the people at large rather than by particular contractors subject to a demand for a massive forfeiture. As the government itself argued in its *Reynolds* brief, when a government claim is lost by virtue of the state-secrets privilege "the public is left in no worse position" than if the government had never brought its claim in the first place. 1952 WL 82378, at *17.

At the same time, a ruling by this Court that the Contractors are the moving parties for privilege purposes would infuse government contracts with damaging uncertainty. Government contractors are often trusted to deal with – indeed, to develop –

process and can draw on "personal knowledge"); 48 C.F.R. § 33.214 (contrasting contracting officer with "neutral person"). *Compare United States v. Wunderlich*, 342 U.S. 98, 99-100 (1951) (holding, prior to enactment of the Contract Disputes Act or its predecessor, that government contractor contracted away the right to review of an adverse government decision).

secret technology.[11] Their efforts are critical to the national defense. *See, e.g.*, 50 app. U.S.C. § 2071 (discussing importance of contracts that promote "national defense"); U.S. GAO, GAO-10-317R, *DOD Assessments of Supplier-Base Availability for Future Defense Needs* 1 (2010) ("The Department of Defense . . . relies on thousands of suppliers to ensure that it has the weapons and supporting equipment needed to meet U.S. national security objectives."). They are governed by complex regulations that do not allow them to protect themselves by customizing contracts. Inevitably, a ruling endorsing use of the privilege to bar defenses to defaults would destroy confidence in government-contract disputes resolution and lead to a more costly and less efficient contracting process. Some contractors would undoubtedly refuse to do business with the government at all, while others would refuse to enter into risky research and development contracts like the one at issue here – exactly the kinds of contracts that the military uses to stay on the cutting edge. *See United States v. Winstar*, 518 U.S. 839, 913 (1996) (Breyer, J., concurring) (explaining the problems involved in hampering the government's ability "to obtain needed goods and

[11] For this reason, government contractors are hardly likely to try to gain a litigation advantage by placing secret information at risk, or by otherwise threatening to undermine national security. *Cf. Tenet*, 544 U.S. at 10-11. Contractors are well aware of the importance of preventing disclosure of sensitive national defense information, and face serious consequences if they abuse the government's trust. *See, e.g.*, 48 C.F.R. § 42.1501.

services from parties who might otherwise, quite rightly, be unwilling to undertake the risk of government contracting"). Indeed, it was to guard against that evil that Congress enacted the statutes ensuring a full and fair process for addressing government default claims and airing contractor defenses. *See, e.g.*, S. Rep. No. 95-1118, at 4 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5235, 5238 (explaining that Contract Disputes Act is important because "[h]ow procurement functions has a far-reaching impact on the economy of our society and on the success of many major Government programs," and "[t]he way potential contractors view the disputes resolving system influences how, whether, and at what prices they compete for Government contract business").[12] Allowing the government to proceed with its default claim here would undercut the very national security interests that the government seeks to protect when it invokes the state-secrets privilege.

[12] The Contract Disputes Act currently sets forth that process – providing, for example, that the contracting officer decision is entitled to no weight or deference in court. *See supra* pp. 8, 42-43. Its predecessor, the Wunderlich Act, was motivated by similar purposes. *See, e.g.*, H.R. Rep. No. 83-1380, at 4 (1954) (explaining that the absence of a fair dispute resolution system would "render the performance of Government work less attractive to the responsible industries" and would "attract more speculative elements whose bids will contain contingent allowances intended to protect them from unconscionable decisions of Government official[s]").

C. The Equities Support Reversal.

Imposing liability on the Contractors was particularly "unconscionable," 345 U.S. at 12, because of the trial court's findings that (1) the government engaged in unfair gamesmanship using the privilege, and (2) the Contractors would have been able to mount a "persuasive case" at trial on their superior-knowledge defense, even without privileged material, Pet. App. 367a.

1. As an initial matter, there is no dispute about the propriety of the trial court's decision to strip the Contractors of their superior-knowledge defense as a result of the state-secrets privilege. The court accepted the government's contentions that it could not attempt to counter the defense without use of secret information, and that at trial the Contractors' own non-privileged evidence would prove to be "inextricably intertwined" with state secrets that "could not be cordoned off in a safe manner," including the question whether certain secret programs even existed. Pet. App. 371a-73a; *see also, e.g.*, JA 586, 599-608, 629, 721-23, 742-51, 778-81. As the government put it in its papers opposing certiorari, "the courts below correctly found petitioners' superior-knowledge defense unamenable to adjudication." Cert. Opp. 17.[13]

[13] In the trial court, the government vacillated on this issue, depending on how it perceived its interest at the time. *Compare* JA 628 *with id.* at 1013. But the government initially advocated, and ultimately accepted as a basis for its victory, exactly what the court did. *See id.* at 1233-34 ("The Executive Branch has warned us repeatedly that issues involving superior

The trial court arrived at that result only after years of trying every possible means available to proceed with litigation of the superior-knowledge defense without encroaching into protected territory. Among other precautions, the court limited the scope of discoverable information; used security officers and a Sensitive Compartmented Information Facility; and held certain proceedings in a sealed deposition room or courtroom. Pet. App. 246a, 345a & n.2, 356a-61a; 28 C.F.R. § 17.17; Security Procedures Established by the Chief Justice of The United States for the Protection of Classified Information, 18 U.S.C. app. 3 § 9 note; Pet. App. 431a-32a ("To the extent that procedures are available to protect national secrets in a judicial setting, those procedures are in place").

None of these efforts worked. *See, e.g.*, Pet. App. 381a ("Despite everyone's best efforts, the risk of compromising national secrets is too serious to proceed to trial."); *id.* at 369a-70a. Thus, while in many cases "creativity and care" can devise "procedures which [would] protect the privilege and yet allow the merits of the controversy to be decided," *Fitzgerald*, 776 F.2d at 1238 n.3, in this case it was not possible to wall off privileged material while continuing to litigate.

knowledge cannot be litigated safely."); *id.* at 1273 ("the trial court correctly applied the law when it removed the issue of superior knowledge from the case and proceeded to litigate the Government's claim that the contractors were in default"); Cert. Opp. 17.

Nor was it possible for the trial court to review all of the complex secret evidence and make an *in camera* determination about the merits of the superior-knowledge defense, without input from the Contractors about privileged material they never saw. The government apparently did not share the entire universe of secret information with the court. *See* Pet. App. 441a (stating that "privileged information *known to this Court* does not clearly establish that defendant could refute" the Contractors' superior-knowledge showing (emphasis added)). Further, the court found that the Contractors' "superior knowledge claims are too complex to be resolved through a selective *ex parte, in camera* examination of evidence." *Id.* at 442a. Instead, "[t]he nature of the information involved likely would preclude the court from finding facts with the degree of certainty that justice requires." *Id.*; *see also id.* at 441a ("The information concealed by the state secrets privilege is such that its effect on the merits is not readily apparent.").

For these reasons, the trial court concluded that it was simply not possible to adjudicate the superior-knowledge defense. In the absence of "numerous layers of potentially dispositive facts," doing so would "lead to an incomplete record on which rulings . . . would be a sham" and an "affront to our system of justice." *Id.* at 379a-80a; *see also id.* at 367a (expressing concern that the government would be "unfairly prejudiced"); Cert. Opp. 17-18 (quoting the trial court's conclusion that "it is not proper to consider [the Contractors'] *prima facie* evidence

when [the government] might refute" that evidence "with greater access"); JA 1273, 1284-87.

2. But while the principle that motivated the trial court's decision not to adjudicate the defense was correct, the court applied the principle in precisely the "unconscionable" manner that *Reynolds* and its progeny forbid. The relevant question is not simply whether the superior-knowledge *defense* could be litigated. It is whether the government's default claim *as a whole*, of which the superior-knowledge defense was a critical aspect, could go forward once the Contractors were deprived of their ability to defend themselves. Under the authorities discussed above, the answer is plainly no. Rather, the only result consistent with fundamental fairness and due process is entry of judgment for the Contractors.

That result is particularly justified because the trial court found that the government was engaged in exactly the kinds of abuses that the *Reynolds* rule guards against. General Dynamics is not privy to the confidential submissions and briefings the government made to the trial court. But the court was able to determine that the government was using secret information for its own "tactical purposes" while refusing to turn the very same information over to the Contractors. JA 524; *see also, e.g.*, *id.* at 550-51 (noting that "sensitive information was used not only to argue Secretary Donley's invocation of the state secrets privilege, but also for defendant's earlier litigation needs," and warning the government that its "tactics raise[d]

serious implications under Rule 11"); Pet. App. 357a-58a nn.9&10 (explaining that the government used information withheld as privileged "in developing [its] defense to superior knowledge claims," and that the court "issued sanctions against the United States" for misrepresentations regarding privileged information); *id.* at 376a (noting "[u]nauthorized disclosures and questionable use of classification procedures by the Government").

The court also observed that the government possessed tremendous power to manipulate the outcome of litigation on the defense. By strategically "timing" its continuing objections to particular aspects of the superior-knowledge inquiry, so as to "cease discovery or testimony," the government could unilaterally "determine who among the litigants would be damaged." *Id.* at 370a; *see also id.* ("The Executive's job is to protect its secrets; it has no obligation to find the truth"); *id.* at 373a ("the Government's incentive would be to expand the inquiry" into privileged areas); JA 493-94. The government should not be permitted to exact a forfeiture based on such improper behavior.

3. Imposing default liability on the Contractors was also particularly inequitable because they were found to have made a strong showing on their defense, even without resort to privileged evidence. After reviewing declarations and other evidence submitted by the Contractors, the trial court repeatedly found that they "could establish a *prima facie* case" – based solely on non-privileged evidence – that the government failed to share its superior

knowledge of the technology involved in developing a stealth aircraft. Pet. App. 441a; *see, e.g., id.* at 367a ("We do not doubt plaintiffs' ability to present a persuasive case based on this information alone."); JA 623 ("[P]laintiffs made an impressive showing that they can present a prima facie case under the existing discovery restrictions imposed by defendant."). In addition, the court found that the "privileged information known to this Court does not clearly establish that [the government] could refute" the Contractors' superior-knowledge defense. Pet. App. 441a.

The government's opposition to certiorari did not question the trial court's rulings that the government had a duty to share its knowledge with the Contractors, or the court's findings that the Contractors had established a *prima facie* valid defense. Indeed, it is well established that the government must disclose "superior knowledge" to a contractor that will otherwise pursue "a ruinous course of action." *Helene Curtis Indus., Inc. v. United States*, 312 F.2d 774, 778 (Ct. Cl. 1963); *see also, e.g., Am. Ship Bldg. Co. v. United States*, 654 F.2d 75, 79 (Ct. Cl. 1981); *Hardeman-Monier-Hutcherson v. United States*, 458 F.2d 1364, 1371-72 (Ct. Cl. 1972) (explaining that "the Government has an affirmative duty to disclose [superior] knowledge" and "cannot remain silent with impunity"). The duty to disclose applies prior to the submission of a bid as well as during performance of the contract, and breach of the duty can function as a complete defense to default termination. *See, e.g., Fla. Engineered Constr. Prods. Corp. v. United States*, 41 Fed. Cl.

534, 542 (1998); *In re Johnson Elecs., Inc.*, A.S.B.C.A. No. 9366, 65-1 BCA ¶ 4628, at 22,107 (holding that because of the government's breach of its superior-knowledge duty "the contracting officer's termination of the contract for default was not proper"); *In re Johnson & Son Erectors*, A.S.B.C.A. No. 24564, 81-1 BCA ¶ 15,082, at 74,602 (collecting cases). The duty applies to both classified and unclassified information, as the trial court correctly concluded – particularly where the contractor is already entrusted with development of highly classified materials relating to the same subject matter. *See, e.g., J.A. Jones Constr. Co. v. United States*, 390 F.2d 886, 888, 893 n.14 (Ct. Cl. 1968) (stressing that government was "not free . . . to stand aside and let the bidder be overwhelmed without a warning," and reasoning that "[w]hile some aspects of the Air Forces' [sic] plans undoubtedly were classified, the evidence falls far short of proving that a general warning to plaintiff would have rent the security blanket").[14]

Here, the Contractors made a showing that the government knew the Contractors lacked access to

[14] *See also, e.g., Northrop Grumman Corp. v. United States*, 63 Fed. Cl. 12, 19 (2004) ("The defendant has not demonstrated any basis for this court to create or recognize a compartmented programs or classified information exception to the government's duty to disclose under the superior knowledge doctrine, nor has any court so held."); John Cibinic, Jr., Ralph C. Nash, Jr. & James F. Nagle, *Administration of Government Contracts* 262 (2006); J. William Eshelman & Suzanne Langford Sanford, *The Superior Knowledge Doctrine: An Update*, 22 Pub. Cont. L.J. 477, 485 (1993).

the confidential information possessed by the other bidder, which made a dramatically different bid at a much higher price and with important limitations. In addition, the Contractors' non-privileged evidence showed that the government promised both before and after bids were submitted that it would comply with its duty to share its superior knowledge during contract performance. But it ultimately dribbled out only small amounts of information, and then stopped sharing altogether – and the bits that it did transmit came too late to be useful. *See supra* pp. 3-5; *see also, e.g.*, JA 392, 689-92. The evidence further showed that the Contractors' schedule difficulties were the direct result of the government's failure to disclose. JA 691-92. All of this evidence was highly probative of the Contractors' defense: that the government breached its duty by allowing the Contractors to proceed on a "ruinous course," and by failing to warn them or to attempt to structure the contract to protect them from their lack of knowledge. *Helene Curtis*, 312 F.2d at 778; *see also Snyder-Lynch Motors, Inc. v. United States*, 292 F.2d 907, 910 (Ct. Cl. 1961) (finding breach of superior-knowledge duty where "the Government was remiss" in withholding "information regarding the . . . experience" on a different, similar contract).

The government's assertion of the privilege no doubt prevented the Contractors from obtaining additional evidence that would have bolstered their defense. In particular, the Contractors pressed for, but were unable to obtain, evidence regarding the knowledge the government derived from stealth programs other than the B-2 program – programs so

secret the government refused to confirm or deny their existence. JA 521-22; Pet. App. 370a-73a. But even without resort to state secrets, the Contractors submitted credible evidence sufficient to entitle them to present their defense to the trier-of-fact, had the government's invocation of the privilege not prevented that. *See* Pet. App. 441a-42a; JA 1234-35. Their showing was so persuasive that the trial court stated that they were likely to "establish" their superior-knowledge defense at trial. Pet. App. 369a.

That finding reinforces the conclusion that upholding the government's default claim, without consideration of the superior-knowledge defense, was a sham and a mockery of justice – one that, if allowed to stand, could end up costing the Contractors billions of dollars.

III. The Court Should Order Reinstatement of the Judgment Entered When the Trial Court Converted the Termination to One for the Government's Convenience.

For the reasons set forth above, the government cannot justly pursue its default claim, and this Court should rule that the Contractors are entitled to judgment in their favor on default. That will ensure that the government cannot penalize the Contractors on the basis of an alleged default that, through no fault of their own, they have been prevented from disproving.

But the Court should do more to bring this case to a just conclusion: it should remand with directions to reinstate the judgment entered by the Court of Federal Claims at an earlier stage of the case (before

being vacated in the first appeal) when the termination had been converted to a termination for convenience. *See supra* p. 16. Under the governing regulations and the terms of the contract, "[i]f, after termination, it is determined that the Contractor was not in default, or that the default was excusable, the rights and obligations of the parties shall be the same as if the termination had been issued for the convenience of the Government." 48 C.F.R. § 52.249-9(g). A termination for convenience enables the government to end a contract on a no-fault basis without exposure to contract breach damages, but prevents the government from saddling the contractor with unreimbursed costs of work already performed. *See id.* § 52.249-2(g)(2); *see also id.* § 49.201.

Here, after the trial court invalidated the default on the ground that it was pretextual, it applied the rules for terminations for convenience and held that the Contractors could recover their actual unreimbursed performance costs (up to a contractual cap). Pet. App. 341a-42a; *see, e.g.*, John Cibinic, Jr., Ralph C. Nash, Jr. & James F. Nagle, *Administration of Government Contracts* 1120 (2006). If the Contractors are not reimbursed for the amounts they spent performing the contract prior to termination, then the government will have succeeded in imposing an unjust sanction on them as a consequence of the termination decision – precisely the result that the *Reynolds* principle prohibits in this case. Were the rule otherwise, the government could simply time its termination and its contract payments for maximum advantage, as it did here, so

as to ensure that it paid as small an amount of a contractor's costs as possible. Reimbursement of incurred costs eliminates that possibility and fairly accounts for where both parties stood when their contract ended.

In allowing a termination-for-convenience recovery, the trial court addressed the effects of the elimination of the superior-knowledge issue from the case. It ruled that the burden of the parties' inability to address the issue should be split, with the Contractors being barred from showing that they would have earned profits if the government had shared its knowledge and the government being barred from showing that the Contractors would have lost money on the contract if (as the government argued) it had no duty to share its knowledge. *See supra* pp. 14-15. Reinstatement of that Solomonic ruling would resolve this case equitably and without further litigation.

The government may argue, as it has previously, that if the default is overturned, there should be no recovery by anyone – *i.e.*, that "plaintiffs' entire claim" for costs "cannot be decided" due to the effects of the state-secrets privilege. JA 1058. But that outcome would not serve the ends of justice because (1) it would leave the Contractors' actual out-of-pocket expenditures unreimbursed, and (2) if the superior-knowledge issue could have been litigated, the Contractors' recovery is at least as likely to have increased to reflect lost profits as to have decreased to reflect losses they never incurred. In all events, the Court should make clear that on remand there

can be no consideration of reinstating the default determination, as to which the Contractors have a substantial but non-justiciable defense.

CONCLUSION

The Court should reverse the Federal Circuit and rule that the Contractors are entitled to judgment on the default claim. It should also direct reinstatement of the final judgment the Court of Federal Claims entered when the termination had been converted to one for convenience.

Respectfully submitted,

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PETITIONER'S BRIEF

Supreme Court, U.S.
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Nos. 09-1298 & 09-1302

In The Supreme Court of the United States

♦

GENERAL DYNAMICS CORPORATION,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

♦

THE BOEING COMPANY,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent

♦

On Writ Of Certiorari To The United States Court Of Appeals For The Federal Circuit

♦

BRIEF OF PETITIONER THE BOEING COMPANY

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QUESTION PRESENTED

Whether the Due Process Clause of the Fifth Amendment permits the Government to maintain a claim while simultaneously asserting the state secrets privilege to bar presentation of a prima facie valid defense to that claim.

PARTIES TO THE PROCEEDING BELOW

The case caption contains the names of all parties who were parties in the court of appeals.

CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.6, Petitioner states as follows:

As of December 31, 2009, two companies disclose, in filings with the U.S. Securities and Exchange Commission, beneficial ownership of 10 percent or more of the outstanding stock of The Boeing Company: State Street Corporation, a publicly held company whose subsidiary State Street Bank and Trust Company acts as trustee of The Boeing Company Employee Savings Plan Master Trust; and Evercore Trust Company, N.A., which acts as investment manager of The Boeing Company Employee Savings Plan Master Trust and which is a subsidiary of the publicly held Evercore Partners, Inc.

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OPINIONS BELOW

The opinions of the Federal Circuit (Pet. App. 1a-34a, 178a-211a, 250a-79a) are reported at 567 F.3d 1340, 323 F.3d 1006, and 182 F.3d 1319, respectively.[1] The pertinent opinions of the Court of Federal Claims and its predecessor, the Claims Court (Pet. App. 35a-177a, 212a-49a, 280a-342a, 343a-81a, 382a-429a, 430a-43a; Joint Appendix ("JA") 349-72) are reported at 76 Fed. Cl. 385, 50 Fed. Cl. 311, 40 Fed. Cl. 529, 37 Fed. Cl. 270, 35 Fed. Cl. 358, 29 Fed. Cl. 791, and 25 Cl. Ct. 342, respectively. Additional relevant orders of the trial court (JA 388-94, 478-49, 504, 524-25, 550-51, 576-77, 622-25, 640-41, 768-69, 787-90, 793-95, 983-86, and 1233-35) are unpublished.

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JURISDICTION

The Federal Circuit entered judgment on June 2, 2009, and denied the timely petitions for rehearing and rehearing en banc on November 24, 2009. Pet. App. 444a-45a. On January 22 and 28, 2010, and March 11 and 12, 2010, the Chief Justice extended the deadline for filing petitions for writ of certiorari in Nos. 09-1298 and 09-1302, first to March 24, 2010, and then to April 23, 2010, and the petitions were filed on that date. The petitions for writ of certiorari

[1] Unless otherwise specified, all references to the Pet. App. are to the appendix to the petition for certiorari filed in No. 09-1298.

were granted and consolidated on September 28, 2010. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

♦

STATUTORY AND CONSTITUTIONAL PROVISIONS INVOLVED

Federal Rule of Evidence 501, adopted by statute, *see* Pub. L. No. 93-595, § 1, 88 Stat. 1933 (1975), provides in pertinent part that "the privilege of a . . . government . . . shall be governed by the principles of the common law as they may be interpreted by the courts of the United States in the light of reason and experience." The Fifth Amendment to the United States Constitution provides in pertinent part: "No person shall . . . be deprived of life, liberty, or property, without due process of law . . . ."

♦

STATEMENT

A. Factual Background

1. In 1988, the Navy and Petitioners The Boeing Company (then McDonnell Douglas Corporation) and General Dynamics Corporation (the "Contractors") entered into a fixed-price research-and-development contract with the Contractors to develop the "A-12 Avenger," a state-of-the-art, carrier-based, stealth aircraft. Pet. App. 40a. The contract required "two major defense contractors with impeccable credentials and long histories of government service to

undertake a complex and highly sensitive research and development project involving stealth technology." *Id.* at 248a. The Contractors first had to develop a design for the aircraft acceptable to the Navy, and then to manufacture and test eight prototype aircraft of increasing complexity, with the eighth aircraft fully functional. Pet. App. 40a. In May 1990, the Navy exercised an option to purchase six production aircraft ("Lot I"), which were to be delivered between June 1991 and May 1992. *Id.* at 40a-41a.

At the time of the contract, "the Air Force already had conducted flight tests for the B-2 Bomber and the F-117A Fighter," both of which employed stealth technology, and "[t]he A-12 was designed to apply similar technology." *Id.* at 353a. The trial court found that the Contractors "were anxious to access B-2 and F-117A program information during contract performance, and they had reason to expect that they would be granted such access." *Id.* at 353a-54a. Indeed, the court found that "[t]he Government contemplated sharing information with the contractors." *Id.* at 354a n.6. For example, the court noted, "the Navy and the Air Force were directed to form a joint committee" so that the Navy's A-12 program could "take advantage of previous technologies developed by the USAF and minimize life cycle costs." *Id.* (quotation marks omitted).

In testimony credited by the trial court, Secretary of the Navy John Lehman emphasized the importance of sharing the Air Force's stealth technology with the A-12 program:

> "[T]here was an unquestioned assumption when we started the [A-12] program that [the Navy] would have full and unimpeded access to all of the B-2 technology. . . . [S]ince the airplane was to be a miniature B-2, which would face all of the same unstable flight control issues, all of the same wind tunnel expenses, all of the same issues of dealing with engine inlets and outlets, that an enormous amount of money could be saved in wind tunnel time and development process by simply using the Air Force Northrop data."

Id. (quoting Lehman Dep. at 104-05 (July 26, 1995)).

For these reasons, the court found, the Deputy Assistant Secretary of Defense for Procurement, who initially opposed "putting the A-12 out for bids on a fixed-price contract[,] . . . relented only with assurance that the Government would share its stealth technology with the contractors. Otherwise, she predicted, it cannot be done." *Id.* at 64a n.16.

2. The Contractors commenced performance in January 1988. From the beginning, the Contractors' progress was hampered because "[t]he United States Air Force chose not to share its highly sensitive stealth information sufficiently to avoid technical difficulties and delay," contrary to the mutual expectations and understanding of the Contractors and the Navy. *Id.* at 52a; *see also id.* at n.9 ("The contractors wanted and needed highly sensitive technical information for the A-12, and the Navy wanted them to

have it."). The original schedule required delivery of the first of the eight test aircraft in June 1990, but because the Contractors had been forced essentially to reinvent stealth technology from scratch, it was clear early on that the Contractors would not be able to meet that initial deadline. *Id.* at 37a. The parties discussed, but did not agree upon, a revised schedule; the Contractors "did not want to become contractually bound to a new schedule because of the uncertainties of controlling weight without having the benefit of shared technical information from the Air Force." *Id.* at 70a. In August 1990, the Navy unilaterally issued a contract modification, called P00046, which set a new schedule for delivering the eight test planes but did not establish a schedule for subsequent stages of contract performance (including delivery of the Lot I production aircraft). *Id.* at 4a-5a.

The Contractors continued to perform through the fall of 1990, at a cost to them of $120-150 million per month. *Id.* at 6a. During this period, the parties resolved all outstanding design issues, and the trial court found that "the Navy agreed that technical concerns had been addressed and resolved to its satisfaction. The Navy accepted plaintiffs' design for the A-12 in November 1990." *Id.* at 57a.

During this same period, even as the Contractors and the Navy reached agreement on the design and the Contractors continued to spend $120-150 million per month of their own money, the Department of Defense conducted a review of the A-12 program as part of a larger retrenchment in defense spending

sparked by the end of the Cold War. *See generally id.* at 387a-400a. On January 7, 1991, "[a] $553 million progress payment was due to the contractors." *Id.* at 399a. Over the Navy's objections, Secretary of Defense Cheney decided in early 1991 to withdraw support for the A-12 program, and on Sunday afternoon, January 6, 1991, the Defense Department informed the Navy's contracting officer that it "would not authorize the expenditure or obligation of any more funds to the program." *Id.* at 398a. Accordingly, the next day, the Navy's contracting officer terminated the contract for default rather than make the payment that was due, even though he strongly supported continuing the A-12 program. *See generally id.* at 399a-403a; *cf. id.* at 248a ("For reasons that do not appear in the record of this case in their entirety, the Government abruptly terminated the contractors for default.").

The Navy asserted that the Contractors were in default for "fail[ing] to . . . [p]rosecute the work so as to endanger performance of th[e] contract." 48 C.F.R. ("FAR") § 52.249-9(a)(1)(ii) [JA 223-24]; *see also* FAR § 52.249-8(a)(1)(ii) [JA 217-18]. Specifically, the Navy based the default termination on its projection that the Contractors would not meet the P00046 schedule for the delivery of the eight test planes and would not meet the *original* schedule for delivering the Lot 1 production planes (even though that schedule had been displaced by the P00046 modification,

see Pet. App. 14a).[2] Shortly after the termination for default, the Navy demanded that the Contractors return approximately $1.35 billion in progress payments plus interest.

B. Legal Background: Pertinent Principles of Government Contract Law

In order to place into context the issue on which this Court granted review, it is important to understand certain background principles governing the termination of government contracts, all of which were acknowledged by the courts below and are not in dispute here.

1. When the Government believes that its contracting partner has committed a serious breach of its obligations, the Government can terminate the contract for default. *See, e.g.*, FAR §§ 52.249-9(a)(1) [JA 223-24], 52.249-8(a)(1) [JA 217-18]. To do so, the Government must assert a formal claim against the contractor. As the Acting Solicitor General has acknowledged, *see* Br. for the United States in Opp'n in Nos. 09-1298 and 09-1302 ("Opp.") at 13-14, default

[2] The Government also asserted that the Contractors were in default for failing to meet the original contract design requirements, but the trial court found that the Navy had accepted a modified design in November 1990, Pet. App. 57a, and the Government did not appeal that ruling. Accordingly, as the case comes to this Court, the sole ground upon which the default termination rests is the Contractors' failure to make progress toward timely completion of contract performance.

termination is "a government claim," *Malone v. United States*, 849 F.2d 1441, 1443 (Fed. Cir. 1988), for it is an "assertion" by the Government "seeking, as a matter of right, . . . relief arising under or relating to the contract," FAR § 52.233-1(c) (defining "claim"); *see also* FAR § 2.101(a) (same).

According to the Contract Disputes Act's unique procedures governing the termination of government contracts, the Government must first submit its default termination claim to its own contracting officer, who will, if he determines that default termination is appropriate, issue an administrative decision terminating the contract for default. 41 U.S.C. § 605(a) ("All claims by the government against a contractor relating to a contract shall be the subject of a decision by the contracting officer."); *Malone*, 849 F.2d at 1443 ("A default termination falls precisely within the contours of" § 605(a).); FAR § 33.211. The contracting officer's decision stands as a "final and conclusive" adjudication of the Government's claim, unless the contractor timely appeals that decision to the appropriate agency board of contract appeals or brings a suit challenging that decision in the Court of Federal Claims. 41 U.S.C. §§ 605(b), 609(a)(1); *see also Seaboard Lumber Co. v. United States*, 903 F.2d 1560, 1562 (Fed. Cir. 1990).

If the contractor mounts such a challenge to the default termination, the Government bears the burden of proof. *See, e.g., Lisbon Contractors, Inc. v.*

United States, 828 F.2d 759, 763-65 (Fed. Cir. 1987). The Federal Circuit has explained:

> The default termination order is deemed by the [agency boards of contract appeals] to be a decision by the contracting officer on a government "claim" against the contractor which, being adverse, the contractor may appeal to the board under the [Contract Disputes Act]. . . . [Accordingly,] the imposition of the burden of proof of default . . . falls naturally on the government inasmuch as the government is only being made to bear the burden of proof on its own "claim" of default.

Id. at 764.[3] The courts below acknowledged and applied these rules, and they are not at issue in this Court. *See* Pet. App. 196a (holding that the Government has the burden of proof); *id.* at 269a-70a (same). Functionally, then, the contractor is the defendant-appellant, not the plaintiff.

2. The courts have long considered default termination to be "a drastic sanction" exacting a "severe penalty," *J.D. Hedrin Construction Co. v. United States*, 408 F.2d 424, 431 (Ct. Cl. 1969), that qualifies as a "species of forfeiture" imposed by the

[3] *Lisbon* also held that the same rules apply regardless of whether the contractor appeals the contracting officer's decision to the appropriate board of contract appeals or seeks review in the Court of Federal Claims, explaining that otherwise, "the government would receive an advantage simply by reason of the choice of forum, a result which finds no support in the statute or Court of Claims precedent." 828 F.2d at 764-65.

Government. *Decker & Co. v. West*, 76 F.3d 1573, 1580 (Fed. Cir. 1996); *see also DeVito v. United States*, 413 F.2d 1147, 1153 (Ct. Cl. 1969) (same); *Schlesinger v. United States*, 390 F.2d 702, 709 (Ct. Cl. 1968) (noting the "drastic consequence" of default termination).[4] If the Government's default termination claim is sustained, the contractor is potentially subject to a number of severe penalties. Most significantly, upon termination for default, the contractor must forfeit payment for all of the costs it has incurred in performing work that had not yet been accepted by the Government. *See* FAR § 49.402-2(a). Not only is the Government relieved from any liability for the contractor's unreimbursed costs incurred performing work that was not yet accepted at the time of termination, it may even seek repayment of unliquidated "progress payments," that is, advance payments to the contractor for such work. *Id.* In addition, a default termination may have severe collateral consequences for the contractor, including suspension or debarment from public contracting, *see* FAR § 9.406-2(b)(1), and loss of future government contract competitions, *see*

[4] Indeed, both the trial court and the court of appeals below recognized that default termination "is a forfeiture that is disfavored in the law and to be construed narrowly by the courts." Pet. App. 114a (quoting *DeVito*, 413 F.2d at 1153); *see also id.* at 190a (noting "judicial aversion to default terminations"); *id.* at 248a (describing the default termination in this case as a "grievous sanction"); *id.* at 229a n.11 ("Termination for default is a very serious sanction that rarely is applied by the Government.").

Bannum, Inc. v. United States, 91 Fed. Cl. 160, 171 (2009).

The default termination sought by the Government in this case would impose severe financial penalties on the Contractors. The trial court found that the Contractors had incurred over $1.2 billion in unreimbursed costs in performing their obligations under the contract. Pet. App. 342a. In addition, as previously noted, shortly after the Navy terminated the contract, the contracting officer demanded that the Contractors return over $1.35 billion in progress payments for work the Navy claimed had not been accepted. *Id.* at 8a. On the same day, the Government and the Contractors entered a Deferment Agreement in which the Government "agreed to take no action 'to enforce collection of the amount demanded' pending action by the court." JA 366. Interest has therefore accrued on these amounts since June 1991, bringing the total forfeiture sought by the Government in this case to more than $5 billion.

3. In cases in which there has been no serious breach by the private contractor, the law provides the Government with an option for terminating its contracts at will. As the Acting Solicitor General has explained, *see* Opp. at 5 n.3, the Government has long enjoyed "[t]he right to terminate a contract when there has been no fault or breach by the non-governmental party . . . for the 'convenience' of the government." *Maxima Corp. v. United States*, 847 F.2d 1549, 1552 (Fed. Cir. 1988). This right, which is uniquely held by the Government, safeguards the

Government's resources by permitting the Government at any time to walk away from its contractual obligations without liability for breaching the contract. When the Government terminates a contract for convenience, the contractor ordinarily is entitled only to payment of "[1] costs incurred, [2] profit on work done and [3] the costs of preparing the termination settlement proposal." *Id.* Unlike a private party who walks away from a contract, however, the Government is not obligated to pay the anticipated profits on work that remains to be done when it terminates the contract for its convenience. *Id.*; *see also* FAR § 52.249-2(f) [JA 207-09].

The parties agree that if the Contractors prevail here and the default termination of the A-12 contract is not sustained, "the court may treat the termination as one for the convenience of the government," with the result that the Government walks away without liability for breach, as described above. Opp. at 5 n.3 (citing *Maxima Corp.*, 847 F.2d at 1553); *see* FAR §§ 49.401(b), 52.249-9(g) [JA 226]. As explained below, however, a termination for convenience in this case will put the Government in an even more favorable position than the generous result this option ordinarily affords it. Specifically, the Government's invocation of the state secrets privilege has barred the Contractors from pressing a claim for their profit on the work that was completed before termination (i.e., the second category of payment ordinarily made to a contractor following a termination for the convenience of the Government). *See infra* at 16-20.

C. Litigation History

1. As required by the Contract Disputes Act, *see* 41 U.S.C. § 605(a), the Government's default termination claim was initially resolved by the contracting officer. *See* JA 353-70 (holding that the contracting officer's default termination notice, the demand for the return of the $1.35 billion in progress payments, and the Deferment Agreement constituted a final decision on the Government's default termination claim). In accordance with the statute, *see* 41 U.S.C. § 609(a)(1), the Contractors sought review of the contracting officer's decision by filing this suit. While the Contractors thus were the nominal plaintiffs in the trial court in this case, their status simply reflects the unusual, Government-friendly procedural framework established by the Contract Disputes Act for resolving default termination claims. As discussed above, the statute allows the Government to enter an administrative judgment in its own favor on its default termination claim that will bind the contractor and entitle the Government to impose the above-described sanctions against it unless it appeals to the appropriate agency board of contract appeals or brings an action challenging the administrative determination in the Court of Federal Claims. *See* 41 U.S.C. §§ 605(b), 609(a)(1).

From the outset, the Contractors asserted that the delays experienced in the A-12 program were attributable to the Government's failure to timely share its "superior knowledge" – specifically, the critical "stealth" technology data the Air Force had

developed in connection with the B-2 and F-117A programs. "It is well settled . . . that where the Government possesses special knowledge, not shared by the contractor, which is vital to the performance of the contract, the Government has an affirmative duty to disclose such knowledge." *Hardeman-Monier-Hutcherson v. United States*, 458 F.2d 1364, 1371-72 (Ct. Cl. 1972); *see also* Pet. App. 270a ("[t]his doctrine of superior knowledge is well established in law"); *GAF Corp. v. United States*, 932 F.2d 947, 949 (Fed. Cir. 1991); *Helene Curtis Indus., Inc. v. United States*, 312 F.2d 774, 777-79 (Ct. Cl. 1963). The Contractors thus contended that the Government's failure to share its superior knowledge not only precluded the default termination, but also required, once the default termination was converted to a termination for convenience, an equitable adjustment to the contract price that would allow recovery of a reasonable profit on the work completed.[5] The Contractors' superior knowledge contentions were thus two-fold, constituting both a defense to the Government's default termination claim and also an affirmative claim for additional recovery from the Government

[5] As discussed above, a contractor is ordinarily entitled to recover both its costs and a reasonable profit on the work completed when a default termination is converted into a termination for convenience. In this case, however, Congress had not fully funded the contract before termination, and the trial court concluded that the Contractors' overall recovery was limited to the amount obligated by Congress absent an equitable adjustment. *See* Pet. App. 349a-50a; *id.* at 282a-84a.

beyond costs if the default termination were converted into a termination for convenience.

From very early in the litigation, the Government strictly limited discovery of information relating to the B-2 and F-117A programs. *See* JA 383-87. And although the Government claimed that the Contractors had access to these and *other* highly classified programs that involved stealth technology, it refused to allow any discovery at all related to these other programs. *See* JA 516, 520-23; JA 631-38; JA 974, 979-80.

In 1993, the Government moved to dismiss the Contractors' superior knowledge defense to the default termination and their claim for an equitable adjustment of the contract price, arguing that the state secrets doctrine barred litigation of these issues. In support of its assertion of the state secrets privilege, the Government invoked a declaration previously submitted by then-Secretary of the Air Force Donald Rice in support of the discovery limitations it had imposed earlier, and later supplemented it with additional declarations from General Merrill A. McPeak (at the time serving as Acting Secretary of the Air Force) and Acting Secretary of the Air Force Michael B. Donley. *See* Pet. App. 358a, 373a-75a. These declarations emphasized the "'*extremely grave damage to the national security*'" that could be reasonably expected to flow from unauthorized disclosure of "'the stealth technology from classified, special access programs, such as the B-2 or F-117A.'"

Pet. App. 375a (quoting Rice Declaration) (emphasis added by the court).

Nevertheless, the trial court found that the Contractors had "made an impressive showing that they can present a prima facie case under the existing discovery restrictions imposed by defendant [allowing access to the B-2 and F-117A information subject to strict limitations]. The unavailability of certain information does not require dismissal because plaintiffs have shown that they can proceed with the information available." JA 623; *see also* Pet. App. 441a ("We ruled that plaintiffs could establish a *prima facie* case, and that privileged information known to this court does not clearly establish that defendant could refute that showing."). Based on that showing, the trial court permitted limited discovery under stringent security procedures, but ultimately terminated the discovery after a number of security problems arose. *See id.* at 357a-61a.[6]

[6] It is important to note that the trial court repeatedly found that the security problems were not caused by the Contractors, but rather arose at least in part from the improper actions of Government litigation counsel. Indeed, at one point the court entered sanctions against the United States (though the court later removed them after the Assistant Attorney General represented that he would take corrective action). *See, e.g.*, Pet. App. 357a-58a & nn.9-10; *id.* at 376a (citing "[u]nauthorized disclosures and questionable use of classification procedures by the Government"); *id.* at 433a n.1; JA 623 n.1 (responsibility for "improper disclosures of sensitive information . . . cannot be placed on plaintiffs").

2. In 1996, the trial court held that the default termination could not be sustained because it had been pretextual, and the contracting officer had not exercised reasoned discretion in invoking this draconian remedy. Accordingly, the trial court converted the termination for default into a termination for the convenience of the government. *See id.* at 382a-429a. As noted above, when a contract is terminated for the convenience of the government, the contractor is ordinarily entitled to payment of "[1] costs incurred, [2] profit on work done and [3] the costs of preparing the termination settlement proposal." *Maxima Corp.*, 847 F.2d at 1552. The Court of Federal Claims awarded the Contractors $1.2 billion in unreimbursed costs, *see* Pet. App. 280a-342a, but refused to award profit on the work the Contractors had done because the state secrets doctrine prohibited the Contractors from proceeding with their affirmative superior knowledge claim for an equitable adjustment of the contract price. *Id.* at 353a-81a.

As the trial court explained, the Contractors argued that "once they have proven their superior knowledge-based claim, corresponding equitable adjustments would increase the price of the A-12 contract enough to avoid the imposition of a loss ratio and entitle them to profits." Pet. App. 353a.[7]

[7] If the Government can prove that "the contractor would have sustained a loss on the entire contract" when it terminates a contract for convenience, a contractor cannot recover the profits on the work completed to which it would otherwise be

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In response, the Government argued (i) "[t]he present state of superior knowledge discovery does not verify plaintiffs' allegations," and (ii) "[e]ven if it did, further inquiry into various [other] 'black' programs would undermine plaintiffs' argument." Pet. App. 353a. In particular, the Government argued that the Contractors' alleged "participation in other highly classified Air Force programs" – information as to which the Government had asserted the state secrets privilege and thus barred discovery – provided them with "information and experience that negate a credible superior knowledge claim." Pet. App. 355a.[8]

entitled, and even its recovery of its out-of-pocket costs may be limited. Pet. App. 347a; *see also* FAR § 49.109-7(a). The amount of the loss on the entire contract proved by the Government is applied pro rata to the unreimbursed costs through a loss ratio. *See* Pet. App. 347a-48a.

[8] Because the Contractors do not have access to the privileged information or the Government's *ex parte* submissions to the trial court, their understanding of the privileged information and the Government's arguments is based on what appears in the trial court's opinions. As discussed in the text, it appears from the trial court's description that the information as to which the Government asserted the state secrets privilege relates to highly classified programs, other than the B-2 and F-117A programs to which the Contractors were ultimately granted access (though not in time to avoid the costs and delays that resulted from the Government's failure to share this information in a timely manner). *See* Pet. App. 354a. But the Government's apparent claim that the Contractors had access to these other programs and, through this access, could have obtained substantially the same technology that they sought from the B-2 and F-117A programs is implausible on its face. Even if it were true that some personnel employed by the Contractors had timely access

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The Court of Federal Claims rejected the first argument, again finding (as it had in 1993, *see* JA 623) that the Contractors had the "ability to present a *prima facie* case based on A-12 program information alone." Pet. App. 373a; *see also id.* at 367a ("Plaintiffs have maintained that they could prove superior knowledge within the confines of the programs to which they have been given access. That may be true. We do not doubt plaintiffs' ability to present a persuasive case based on this information alone."); *id.* at 441a ("We ruled that plaintiffs could establish a *prima facie* case, and that privileged information known to this court does not clearly establish that defendant could refute that showing."). But the court found that the Government's second argument – that the Contractors' "participation in other highly classified Air Force programs" provided them with "information and experience that negate a credible superior knowledge claim," *id.* at 355a – could not be safely litigated without endangering state secrets concerning both the B-2 and F-117A programs and the other "black" programs to which the Contractors allegedly had access. *Id.* at 367a-81a.

to these programs, in light of the highly classified and compartmented nature of the programs, there is simply no way that any technology from those programs could have been lawfully transferred to the A-12 program without the Government's express consent. It is difficult to take seriously any suggestion that such consent might have been forthcoming at the same time that direct access to the B-2 and F-117A programs was being denied

The court reasoned that each side would have to seek "evidence of plaintiffs' exposure to relevant information through involvement with non-A-12 programs." *Id.* at 369a. Inevitably, according to the trial court, "[t]he Executive necessarily would block the parties' probing at some point, and such an invocation of the military and state secrets privilege would cease discovery or testimony. The timing of the privilege would determine who among the litigants would be damaged." *Id.* at 369a-70a. Compounding the court's concern, "[u]nauthorized disclosures and questionable use of classification procedures by the Government have added to a general unease about litigating plaintiffs' equitable adjustment claims [based on the Government's superior knowledge] further." *Id.* at 376a.

In these circumstances, the court concluded, "[w]e cannot know fully the effects that privileged information omitted from evidence would have for the parties in this case. . . . [W]e are satisfied that trying this case would lead to an incomplete record on which rulings by the trial court and consideration by the Federal Circuit on appeal, would be a sham." *Id.* at 379a-80a. Accordingly, the court held that the Contractors could not seek profits and the Government could not seek to reduce the Contractors' recovery of costs by application of a loss ratio. *Id.* at 380a-81a.

3. On appeal, the Federal Circuit reversed the trial court's holding that the termination for default had been pretextual. *Id.* at 259a-70a. The court of

appeals remanded for determination of whether the Government could prove that the Contractors were in default. *Id.* at 269a-70a. As a result of that ruling, the court held that the issues surrounding the Contractors' superior knowledge claim were "not ripe for our decision." *Id.* at 271a.

The court of appeals further observed that "[b]ecause of the passage of time and of possible intervening developments, we are in no position to judge whether the risk of disclosure of state secrets will preclude adjudication, on remand, of Contractors' superior knowledge claim, and the issues of loss adjustment and reasonable profit." *Id.* Accordingly, the court held that the trial court was "free to reconsider this issue on remand," and "express[ed] no view on the trial court's previous ruling on whether these three interrelated issues may be litigated." *Id.* at 271a-72a.

4. On remand in 2001, the trial court sustained the default termination based solely on its finding that the Contractors would not have met the December 1991 "first flight" milestone set by P00046. *Id.* at 218a-28a. The court rejected all other grounds for default termination the Government alleged – including that the Contractors could not meet weight and other design specifications, that the Contractors' financial condition threatened performance, and that the Contractors failed to give adequate assurances of performance. *Id.* at 230a-43a.

The court also refused to permit the Contractors to present their superior knowledge *defense*, reaffirming its 1996 ruling that superior knowledge issues "could not be tried because the resulting threat to national security would not permit it." *Id.* at 243a-44a.[9] During discovery, the Contractors "issued several interrogatories that prompted the United States to invoke again the military and state secrets doctrines." *Id.* at 244a. After reviewing a classified version of the declaration submitted by Secretary of the Air Force F. Whitten Peters, and in light of the earlier McPeak, Donley, and Rice Declarations, the Court of Federal Claims held that "we remain satisfied that superior knowledge issues in this case cannot be litigated safely." *Id.*

The court again acknowledged that "plaintiffs made a persuasive showing that they could prove their claim without the information." *Id.* at 245a. The court's determination that the Contractors had established a prima facie valid superior knowledge defense was never disturbed. The court also observed that the Government claimed that it could rebut the Contractors' superior knowledge defense with evidence concerning knowledge the

[9] As explained above, the Contractors' superior knowledge assertion arose in 1996 in the context of the Contractors' affirmative claim for profits as part of their termination for convenience recovery At issue in the trial court's 2001 decision and the subsequent proceedings in this case, however, was the Contractors' attempt to assert the Government's superior knowledge as a defense to the Government's default termination claim.

Contractors allegedly derived from other black programs. But absent the privileged information, the court concluded: "We can never know enough to make a finding of fact on this issue. That is why we could not try claims or defenses that depend on information that has been removed from this case." *Id.* Moreover, the court explained that it could not "establish that the information that has been removed from this case would have benefitted either party. Without extensive discovery related to this information, which will not be permitted for years if ever, no one can know whether either party would have been helped or harmed by it." *Id.* Accordingly, the court held that the Contractors "may not use superior knowledge as a defense because we cannot know whether that argument has merit." *Id.* at 246a.

5. On appeal in 2003, the Federal Circuit vacated the judgment sustaining the default termination and remanded, holding that the trial court's finding that the Contractors would not have met P00046's first flight date in December 1991 "[wa]s insufficient to sustain a default termination in this case." *Id.* at 187a. Applying its well-established rule for evaluating default terminations for failure to make progress, the court of appeals instructed the trial court on remand to first "determine[ ] the performance required by the contract and the contract completion date, . . . [and] then decide . . . whether the government has met its burden of proving that the contracting officer had a reasonable belief that there was no reasonable likelihood that the

contractor could perform the entire contract effort within the time remaining for performance." *Id.* at 196a.

Turning to the superior knowledge defense, the Federal Circuit rejected the Contractors' argument that the Government could not, consistent with due process, both continue to assert its claim for default termination and also invoke the state secrets privilege to foreclose the Contractors' superior knowledge defense to that claim. *Id.* at 207a-10a. The court of appeals concluded that the rule established in *United States v. Reynolds*, 345 U.S. 1, 12 (1953), prohibiting the Government "to undertake prosecution and then invoke its governmental privileges to deprive the accused of anything which might be material to his defense," does not extend to this civil claim by the Government seeking the "drastic sanction" of default termination. *See id.* at. 208a (asserting that the Contractors' argument "essentially conflate[s] rules governing criminal and civil proceedings, elevating this civil contract dispute into the constitutional territory of a criminal prosecution"). The court of appeals reasoned that the Contractors "are not at jeopardy from an attack on them by the government," *id.* at 208a, notwithstanding the $5 billion forfeiture the Government would seek. Asserting that the Contractors are "the plaintiffs in this purely civil matter, suing the sovereign on the limited terms to which it has consented," *id.* at 208a, the court held that "the Fifth Amendment does not require that [the Contractors] be able to present

all defenses, including a defense that would threaten national security." *Id.* at 208a-09a.

6. On remand, the Court of Federal Claims in 2007 found that "[t]he contract had no completion date at termination, seemingly leaving the court without a basis for finding a reasonable belief on the part of the contracting officer that the contractors would not complete the work on time." *Id.* at 164a. Nonetheless, the court upheld the default termination based on its finding that the contracting officer could reasonably conclude that the Contractors "were behind schedule at termination according to a self-contained series of milestones, *not in relation to the entire contract*," *id.* at 129a (emphasis added), as the court of appeals' 2003 decision in this case had required, *see id.* at 196a. Given the Federal Circuit's 2003 decision affirming the trial court's earlier holding that the Contractors were barred from presenting their superior knowledge defense, the trial court did not address that issue further. The court entered judgment for the Government sustaining its default termination claim.

7. The Federal Circuit affirmed in 2009. *Id.* at 1a-34a. Concluding that the analysis that its 2003 decision had mandated "cannot be strictly applied," *id.* at 29a; *but cf. id.* at 192a-93a, the court of appeals adopted and applied a new "ad hoc, factual inquiry." *Id.* at 20a-21a. The court's new test required that a default termination for failure to make progress toward timely completion be upheld, even absent a

contract completion date, if the Government shows that, in light of "all relevant circumstances," "the contracting officer was reasonably justified in feeling insecure about the contractors' rate of progress." *Id.* at 27a. The court held that the Government had satisfied this standard and sustained the Government's termination for default claim. *Id.*

The 2009 panel did not revisit the Federal Circuit's 2003 decision barring the Contractors from presenting their superior knowledge defense.

♦

SUMMARY OF ARGUMENT

In this case, the Government asserted a default termination claim against the Contractors, seeking to impose a multi-billion-dollar sanction. The courts below prohibited the Contractors from presenting their prima facie valid superior knowledge defense to that claim because the Government maintained that the defense could be rebutted by the information protected by the state secrets privilege and because the trial court found that litigating the issue would create an undue risk that the state secrets would be disclosed. By allowing the default termination claim nevertheless to proceed in these circumstances, the courts below departed from this Court's precedent and violated fundamental principles of common law and due process.

Invoking *United States v. Reynolds*, 345 U.S. 1 (1953), the Federal Circuit ruled that the Contractors

were precluded from asserting their superior knowledge defense to the Government's default termination claim because, "when a properly invoked claim of State Secrets privilege undercuts a civil litigant's opportunity to prove its case, the interests favoring the protection of the state secret always prevail." Pet. App. 210a. But the Contractors do not dispute that genuine state secrets must always be protected, nor are they in a position to dispute the trial court's finding that genuine state secrets would in fact be threatened by litigation of their superior-knowledge defense; rather, Contractors respectfully submit that permitting the privilege to preclude their prima facie valid defense requires dismissal of the Government's default termination claim, as a matter of both the common law governing the state secrets privilege and due process. Neither the Due Process Clause nor basic principles of fairness permit the Government both to assert a claim and then to ensure its own victory by invoking the state secrets privilege to preclude its opponent from interposing such a defense.

In *Reynolds*, the plaintiffs sued the Government in tort and sought disclosure of a classified report withheld under the state secrets privilege. 345 U.S. at 3-5. Upholding the Government's assertion of privilege, the Court distinguished between a criminal defendant and a civil plaintiff asserting a claim for monetary relief against the Government: "[I]n the criminal field, . . . the Government can invoke its evidentiary privileges only at the price of letting the

defendant go free," for "it is unconscionable to allow [the Government] to undertake prosecution and then invoke its governmental privileges to deprive the accused of anything which might be material to his defense." *Id.* at 12. But this "rationale has no application," the Court held, "in a civil forum where the Government is not the moving party, but is a defendant only on terms to which it has consented." *Id.*

Relying on this discussion in *Reynolds*, the Federal Circuit held that the Contractors had "conflate[d] rules governing criminal and civil proceedings, elevating this civil contract dispute into the constitutional territory of a criminal prosecution." Pet. App. 208a. Concluding that "[t]he Contractors are not at jeopardy from an attack on them by the government," the court ruled that due process did not foreclose the Government from proceeding with its default termination claim, even as the Contractors were barred from presenting their prima facie valid superior knowledge defense. *Id.*

But the Federal Circuit misread *Reynolds*. *Reynolds* did not specifically resolve the situation here, where the Government *is* the "moving party" asserting a *civil* penalty claim against a private party. And contrary to the Federal Circuit's decision, the Contractors *are* at jeopardy – from a staggering multi-billion-dollar forfeiture. The concerns about fairness and integrity that underlay *Reynolds* do not depend upon the happenstance of the label affixed in the litigation to the party bringing the claim. *Reynolds*

notably spoke of the "moving party," not the "plaintiff." 345 U.S. at 12.

In fact, *Reynolds*' rationale concerning criminal defendants plainly applies here: just as it is unconscionable to allow the Government both to prosecute a criminal defendant and "invoke its governmental privileges" to prejudice the defense to the charge, *id.*, it is unconscionable to allow the Government to assert a civil claim against the Contractors that could subject them to a multi-billion-dollar sanction and also invoke the privilege to bar them from litigating a prima facie valid defense to that claim. The underlying risk to the judicial process in both cases is the same: if the Government can both assert a claim and invoke the privilege in a manner that substantially prejudices the defense to that claim, it can distort the court's fact-finding process to its advantage. In both contexts, due process and basic fairness require dismissal of the Government's claim.

Applying *Reynolds* in this way to this case is entirely consistent with other well-established precedent, in which this Court has unambiguously held that due process guarantees a civil defendant "an opportunity to present every available defense." *E.g.*, *Philip Morris USA v. Williams*, 549 U.S. 346, 353 (2007) (quotation marks omitted); *see also Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 429 (1982). As this Court has explained, "[t]he purpose of an adversary hearing is to ensure the requisite neutrality that must inform all governmental decision-making. That protection is of particular importance here, where the

Government has a direct pecuniary interest in the outcome of the proceeding." *United States v. James Daniel Good Real Prop.*, 510 U.S. 43, 55-56 (1993). The Federal Circuit's state secrets ruling thus violates due process and conflicts with this Court's clear teaching.

Except for the ruling below, the Circuit courts have consistently recognized that a civil claim may not proceed where invocation of the state secrets privilege precludes presentation of a valid defense to that claim, or where defending against that claim would run an unacceptable risk of compromising the state secrets. *See, e.g.*, *Mohamed v. Jeppesen Dataplan, Inc.*, 614 F.3d 1070, 1087-90 (9th Cir. 2010) (en banc); *El-Masri v. United States*, 479 F.3d 296, 306-07 (4th Cir. 2007); *Tenenbaum v. Simoni*, 372 F.3d 776, 777 (6th Cir. 2004); *Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1143 (5th Cir. 1992); *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 547 (2d Cir. 1991); *Molerio v. FBI*, 749 F.2d 815, 825 (D.C. Cir. 1984) (Scalia, J.); *cf. Farnsworth Cannon v. Grimes*, 635 F.2d 268, 276 (4th Cir. 1980) (en banc) (per curiam). These decisions are rooted in the broader principle – which the Government has repeatedly and successfully invoked when it found itself, like the Contractors here, *defending* against an affirmative claim for relief – that when the need for safeguarding state secrets substantially prejudices a litigant's ability to defend, relief on the moving party's claim must be denied, for any other course threatens to compromise the integrity of the judicial

process. Only by withholding adjudication of the claim altogether can the court ensure that it does not, itself, become the instrument of an injustice by awarding relief where none was warranted. *See, e.g.*, *Molerio*, 749 F.2d at 825 (Scalia, J.) (it would have been "a mockery of justice for the court – knowing the erroneousness – to participate in that exercise"). This principle applies with special force where the Government is the party asserting the claim, for in that circumstance the Government holds the unique power both to wield the sword of its claim and to simultaneously deprive its opponent of the shield of its defense.

◆

ARGUMENT

The state secrets privilege is a common-law evidentiary rule that shields military, intelligence, and diplomatic secrets from discovery when disclosure of those secrets would harm national security. *See United States v. Reynolds*, 345 U.S. 1, 6-7 (1953); *Molerio v. FBI*, 749 F.2d 815, 820-21 (1984) (Scalia, J.).[10] Although the privilege in this country appears to

[10] Apart from its common-law origins, the state secrets privilege also appears to serve a function of constitutional significance, for it allows the Executive Branch to protect information the secrecy of which is necessary to its Article II military and foreign-affairs responsibilities. *See United States v. Nixon*, 418 U.S. 683, 710-11 (1974); *El-Masri v. United States*, 479 F.3d 296, 303 (4th Cir. 2007).

have roots extending back at least to Aaron Burr's trial for treason, *see United States v. Burr*, 25 F. Cas. 30 (C.C.D. Va. 1807); *Reynolds*, 345 U.S. at 9, the seminal modern decision recognizing and delineating the privilege is *Reynolds*.

As this Court explained in *Reynolds*, the state secrets privilege "belongs to the Government and must be asserted by it; it can neither be claimed nor waived by a private party." *Id.* at 7. The privilege is absolute; once properly invoked, "even the most compelling necessity cannot overcome the claim of privilege if the court is ultimately satisfied that military secrets are at stake." *Id.* at 11.

When the Government asserts this privilege, a court must perform a three-part analysis. First, it must determine whether the procedural requirements for invoking the privilege have been satisfied. *See id.* at 7-8. Most important, "[t]here must be a formal claim of privilege, lodged by the head of the department which has control over the matter, after actual personal consideration by that officer." *Id.* (footnotes omitted). Second, "[t]he court itself must determine whether the circumstances are appropriate for the claim of privilege, and yet do so without forcing a disclosure of the very thing the privilege is designed to protect." *Id.* at 8 (footnotes omitted). Finally, if the first two requirements are satisfied, the court must then determine how – and whether – the case should proceed in light of the successful invocation of the privilege. *See id.* at 11-12. While in some situations

the case can simply proceed without the privileged evidence, in other cases dismissal is required. *See id.*

Reynolds provides clear guidance regarding the first two parts of this analysis, and the Contractors do not dispute their proper application in this case. Rather, this case turns on the third part of the analysis – the consequences of the Government's successful invocation of the privilege. As demonstrated below, both due process and the common-law principles governing the state secrets privilege make clear that a civil claim may not proceed where the Government's invocation of the state secrets privilege substantially prejudices a litigant's ability to defend against that claim. But whatever the precise contours or outer limits of this principle, this Court should hold that, at a minimum, the Government may not assert a claim seeking serious sanctions against a private party and then ensure its own victory by invoking the state secrets privilege to prevent the private party from presenting a prima facie valid defense that could defeat the claim.

THE GOVERNMENT MAY NOT PROCEED WITH A CIVIL CLAIM WHEN THE STATE SECRETS PRIVILEGE BARS A PRIMA FACIE VALID DEFENSE TO THAT CLAIM.

A. This Court Has Held That the Government May Not Pursue a Claim Where Its Assertion of the State Secrets Privilege Substantially Prejudices the Defense.

In *Reynolds*, this Court embraced lower court decisions holding that "in the criminal field . . . the Government can invoke its evidentiary privileges only at the price of letting the defendant go free." 345 U.S. at 12. As the Court explained, the rationale of these cases "is that, since the Government which prosecutes an accused also has the duty to see that justice is done, it is unconscionable to allow it to undertake prosecution and then invoke its governmental privileges to deprive the accused of anything which might be material to his defense." *Id.* Thus, "[t]he burden is the Government's, not to be shifted to the trial judge, to decide whether the public prejudice of allowing the crime to go unpunished is greater than that attendant upon the possible disclosure of state secrets and other confidential information in the Government's possession." *Jencks v. United States*, 353 U.S. 657, 672 (1957).[11]

[11] Consistent with these decisions, the subsequently enacted Classified Information Procedures Act ("CIPA"), 18 U.S.C. app. 3 §§ 1-16, provides that, in the criminal context, "[i]f no adequate substitution can be found [for admissible classified information

(Continued on following page)

To be sure, the Court in *Reynolds* stated that this principle "has no application in a civil forum *where the Government is not the moving party*, but is a defendant only on terms to which it has consented." 345 U.S. at 12 (emphasis added). But the Court's careful framing implicitly acknowledged that this principle *would* apply in a civil forum where the Government *is* the moving party. Indeed, in its brief in *Reynolds* the Government expressly distinguished that case from civil cases "in which discovery is sought against the United States *as plaintiff*." Br. for United States at 66, *United States v. Reynolds*, 345 U.S. 1 (1953) (emphasis added), *available at* 1952 WL 82378. As the Government explained:

> [W]here the Government is plaintiff, as in criminal cases where it is prosecutor, the choice of seeking the aid of the courts by pursuing the action or of refusing to produce is different from that where the Government is defendant. If the Government refuses to produce in the former class of cases, it is denied

that the defendant expects to disclose or cause to be disclosed], the government must decide whether it will prohibit the disclosure of the classified information; if it does so, the district court must impose a sanction, which is presumptively dismissal of the indictment." *United States v. Moussaoui*, 365 F.3d 292, 312 (4th Cir. 2004) (citing 18 U.S.C. app. 3 § 6(e)). If "the court determines that the interests of justice would not be served by dismissal of the indictment," however, the CIPA provides that the court "shall order" other "appropriate" action, such as dismissing a count, finding against the United States on an issue, or excluding testimony. 18 U.S.C. app. 3 § 6(e)(2).

> judicial assistance; but the public is left in no worse position than if it had never instituted the action.

Id. at 17 (footnote omitted). Further, while the threat to life, liberty, and property posed by a criminal prosecution may present the starkest context for application of the principles of due process and fundamental fairness reflected in *Reynolds'* and *Jencks'* analysis, those principles retain substantial force when the Government asserts a civil claim against a private party – especially where, as here, the Government seeks to impose significant punitive consequences in connection with that claim.

B. The Government May Not Pursue Its Default Termination Claim Because Its Invocation of the State Secrets Privilege Foreclosed a Prima Facie Valid Defense to That Claim.

In this case, the Government seeks to impose a civil sanction that could result in one of the largest forfeitures, if not *the* largest forfeiture, in government contracting history – upward of $5 billion. Beyond imposing a punitive monetary sanction, a default termination claim by the Government can also result in unfavorable treatment in, or even disqualification from, future government contract competitions. *See supra* at 10-11. The consequences of a default termination are thus so significant that courts uniformly have called it a "drastic sanction," a "species of forfeiture," that exacts a "severe penalty." *Supra* at 9-10 (citing cases). The courts below acknowledged the

"grievous" nature of such "forfeiture[s]," *supra* at 10 n.4 (citing opinions below), yet they nevertheless allowed the Government to pursue this sanction, even though the Government also invoked the state secrets privilege to prevent the Contractors from presenting and litigating what the trial court's undisturbed findings repeatedly recognized as a prima facie valid defense to the Government's claim. *See* JA 623; Pet. App. 245a, 367a, 373a, 437a, 441a.

In allowing the Government's claim to go forward, the Federal Circuit relied upon the distinction drawn by this Court in *Reynolds* between criminal prosecutions, on the one hand, and civil suits in which "the Government is not the moving party," on the other hand. *Id.* at 208a (quoting *Reynolds*, 345 U.S. at 12). According to the Federal Circuit:

> The Contractors are not at jeopardy from an attack on them by the government. Rather, they are the plaintiffs in this purely civil matter, suing the sovereign on the limited terms to which it has consented. Thus, the Fifth Amendment does not require that they be able to present all defenses, including a defense that would threaten national security. Complying with the high court's edict as we must, we therefore reject the Contractors' Fifth Amendment contention.

Id. at 208a-09a. As demonstrated below, this reasoning was wrong at every turn, for the Contractors *are* at jeopardy – of a multi-billion-dollar forfeiture – from a claim asserted against them *by the Government*.

Under these circumstances, the Fifth Amendment *does require* that they be able to present a prima facie valid defense that could defeat that claim.

1. The Government is the moving party in this case.

It is true, as the Federal Circuit observed, that the Contractors were the nominal plaintiffs in this case. As explained above, however, the caption's nominal structure is simply an artifact of the unusual, Government-friendly framework established by the Contract Disputes Act, *see* 41 U.S.C. § 605(a)-(b), which allows the Government unilaterally to enter an order in its own favor on its default termination claim. "The default termination order is deemed . . . to be a decision by the contracting officer on a government 'claim' against the contractor." *Lisbon Contractors, Inc. v. United States*, 828 F.2d 759, 764 (Fed. Cir. 1987); *see also Malone v. United States,* 849 F.2d 1441, 1443 (Fed. Cir. 1988) (default termination is "a government claim"). The Government's unilateral order binds the contractor and allows the Government to impose sanctions against it, unless the contractor timely appeals that decision to the appropriate agency board of contract appeals or brings a suit challenging that decision in the Court of Federal Claims. *See supra* at 8.

This procedural framework thus shifts the burden of filing suit to the party defending against the Government's claim, but it does not change the fact

that the Government has asserted the underlying claim for relief under the contract, nor does it shift the burden of proof regarding the merits of the default termination, which remains with the Government at all times. *See Lisbon*, 828 F.2d at 764 ("the imposition of the burden of proof of default . . . falls naturally on the government inasmuch as the government is only being made to bear the burden of proof on its own 'claim' of default"); *supra* at 7-9. The Acting Solicitor General has conceded as much. *See* Opp. at 13-14.

The Federal Circuit was thus simply wrong in asserting that the Contractors in this case "are not at jeopardy from an attack on them by the government." Pet. App. 208a. The Government seeks to impose on the Contractors a "drastic sanction" that threatens them with a staggering financial penalty. The core principles of due process and fairness undergirding the Court's analysis in *Reynolds* and *Jencks* surely do not depend on a procedural technicality subject to ready statutory evasion, such as the label applied to each party in an action challenging a default termination. For good reason, then, *Reynolds*' analysis depended not on whether the Government is styled the "plaintiff," but rather on whether it is, in substance, the "moving party." 345 U.S. at 12.

2. Principles of due process and fundamental fairness protect parties defending against civil as well as criminal claims by the Government.

Nor may the decision below be sustained based on the distinction the Federal Circuit drew between criminal and civil proceedings in this context. *See, e.g.*, Pet. App. 208a (asserting that "Contractors essentially conflate rules governing criminal and civil proceedings, elevating this civil contract dispute into the constitutional territory of a criminal prosecution").

Although *Reynolds* discussed the effect of the state secrets privilege when it prevents the litigation of criminal defenses or of civil claims against the Government, it did not directly resolve the case in which the Government's invocation of the privilege substantially prejudices a litigant's ability to defend against a civil government claim. But this Court's analysis in *Reynolds* itself, the Court's due process precedents, a substantial and uniform body of precedent from the Federal Courts of Appeals, the proposed codification of the state secrets privilege, and the judicial treatment of other analogous evidentiary privileges all support a holding that a civil claim brought by the Government should not be allowed to proceed when the Government's invocation of the state secrets privilege would substantially prejudice a litigant's ability to defend against that claim. Simply put, if the Government's assertion of the state secrets privilege requires a litigant to lay down his shield,

basic principles of due process and fundamental fairness require the Government to lay down its sword.

a. When viewed in light of the factors identified by *Reynolds*, a government civil claim against a private party is much more closely analogous to a criminal prosecution than is a civil claim brought against the Government. Whether bringing a criminal prosecution or asserting a civil claim, the Government is clearly the "moving party," employing the truth-finding process and coercive machinery of the courts in attempting to impose a sanction or remedy against a private citizen. In either case, the Government's actions must be tempered by its "duty to see that justice is done," *Reynolds*, 345 U.S. at 12, and it is "unconscionable" for the Government to attempt to subject a private party to judicial coercion of any sort, while at the same time invoking an evidentiary privilege to prejudice substantially the private party's defense, *id.*

Further, when the Government is the moving party asserting a civil claim, it cannot be viewed simply as "a defendant only on terms to which it has consented." *Id.* Indeed, where the Government is a civil plaintiff, the question of sovereign immunity does not even arise. To be sure, the Government is the nominal defendant in this case, for it has enacted a statutory scheme that allows itself unilaterally to enter a judgment in its own favor against the Contractors. But principles of sovereign immunity surely could not shield that judgment from judicial scrutiny,

let alone the Government's attempts to enforce a forfeiture or other sanction against a private party based on that judgment, for it is well settled both that the Government may not rely on sovereign immunity to bar fair and full adjudication of a claim that it has asserted, *see Gardner v. New Jersey*, 329 U.S. 565, 574 (1947) (State waives sovereign immunity by filing proof of claim in bankruptcy proceeding), and also that the Government may not evade judicial scrutiny by forcing otherwise cognizable actions into a forum where sovereign immunity purportedly applies, *see Lapides v. Board of Regents*, 535 U.S. 613, 619-24 (2002) ("the State's action joining the removing of this case to federal court waived its Eleventh Amendment immunity"). *Cf. Battaglia v. General Motors Corp.*, 169 F.2d 254, 257 (2d Cir. 1948) (Congress may not "exercise . . . its control over jurisdiction . . . so . . . as to deprive any person of life, liberty, or property without due process of law"); *Reich v. Collins*, 513 U.S. 106, 109-10 (1994) (similar).

Finally, this Court's solicitude for criminal defendants in *Reynolds* and *Jencks* was plainly driven by the need to vindicate those defendants' fundamental due process right "to present a defense." *Washington v. Texas*, 388 U.S. 14, 19 (1967). But it is well settled that due process protects "civil litigants," as well as those who have been charged with crimes. *Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 429 (1982). Specifically, this Court has long recognized that even in civil cases due process requires that there be "'an opportunity to present every available

defense.'" *Philip Morris USA v. Williams*, 549 U.S. 346, 353 (2007) (quoting *Lindsey v. Normet*, 405 U.S. 56, 66 (1972)); *accord American Sur. Co. v. Baldwin*, 287 U.S. 156, 168 (1932); *cf. Nelson v. Adams*, 529 U.S. 460, 466 (2000) (due process requires "an adequate opportunity to defend against the imposition of liability").

For all of these reasons, basic principles of fairness and due process should apply *whenever* the Government invokes the state secrets privilege to prevent a litigant from interposing a prima facie valid defense, especially when it is the Government itself that has asserted the underlying criminal or civil claim.

b. This result is fully consistent with the well-developed body of precedent from the Federal Courts of Appeals holding that a civil claim may not proceed where the Government's assertion of the state secrets privilege substantially prejudices a civil defendant's ability to defend against that claim.[12] These precedents support dismissal of the Government's default termination claim here.

i. As the Fifth Circuit has recognized, "[m]ost courts that have discussed the state secret

[12] In these cases the Government invoked this principle to bar claims against itself, its officers and employees, and/or its contractors. The same principle should apply a fortiori when the Government presses a claim against a private litigant. *See infra* at 52-54.

privilege have adopted the position that, if the privileged information would establish a valid defense, then the court ought to dismiss the plaintiffs' case." *Bareford v. General Dynamics Corp.*, 973 F.2d 1138, 1143 (5th Cir. 1992) (collecting cases). In the leading case of *Molerio*, for example, the D.C. Circuit held that a plaintiff alleging that the FBI had unlawfully refused to hire him could not pursue his claim when the FBI's invocation of the state secrets privilege barred it from defending its action by proving the "genuine reason for denial of employment." 749 F.2d at 825 (Scalia, J.). The court concluded that without the privileged information that would have allowed the FBI to defeat the claim, any further litigation of the case would have "involve[d] an attempt, however well intentioned, to convince the jury of a falsehood." *Id.* The court thus ruled that the case simply could not proceed: although there may have been "enough circumstantial evidence to permit a jury" to rule in favor of the claimant, it would have been "a mockery of justice for the court – knowing the erroneousness – to participate in that exercise." *Id. Molerio* thus establishes that "summary judgment against the plaintiff is proper if the district court decides that the privileged information, if available to the defendant, would establish a valid defense to the claim." *In re United States*, 872 F.2d 472, 476 (D.C. Cir. 1989) (citing *Molerio*, 749 F.2d at 825); *see also In re Sealed Case*, 494 F.3d 139, 153 (D.C. Cir. 2007) ("If the defendant proffers a valid defense that the district court verifies upon its review of state secrets evidence, then the case must be dismissed.").

Similarly, in *Tenenbaum v. Simoni* the Sixth Circuit affirmed the dismissal of a suit against the United States and various federal employees alleged to have "conducted a criminal espionage investigation of [the plaintiff] Tenenbaum solely because he is Jewish." 372 F.3d 776, 777 (6th Cir. 2004). The court concluded "that Defendants cannot defend their conduct with respect to Tenenbaum without revealing" information as to which the Government had asserted the state secrets privilege. *Id.* "Because the state secrets doctrine thus deprive[d] Defendants of a valid defense to the Tenenbaums' claims," the court affirmed the dismissal of the complaint. *Id.*

Other courts have repeatedly recognized essentially the same rule. *See, e.g.*, *Mohamed v. Jeppesen Dataplan, Inc.*, 614 F.3d 1070, 1083 (9th Cir. 2010) (en banc) ("[I]f the privilege deprives the defendant of information that would otherwise give the defendant a valid defense to the claim, then the court may grant summary judgment to the defendant.") (quotation marks omitted); *Zuckerbraun v. General Dynamics*, 935 F.2d 544, 547 (2d Cir. 1991) ("[I]t has been held that, if the court determines that the privilege so hampers the defendant in establishing a valid defense that the trier is likely to reach an erroneous conclusion, then dismissal is also proper.").

ii. The courts of appeals have also recognized that a claim may not proceed if fully litigating a defense would pose an unacceptable risk of disclosing a state secret. As the Ninth Circuit recently explained:

> even if the claims and defenses might theoretically be established without relying on privileged evidence, it may be impossible to proceed with the litigation because – privileged information being inseparable from nonprivileged information that will be necessary to the claims *or* defenses – litigating the case to a judgment on the merits would present an unacceptable risk of disclosing state secrets.

Mohamed, 614 F.3d at 1083 (emphasis added). Applying this principle, the en banc Ninth Circuit recently upheld the dismissal of claims brought by various individuals alleging that they had suffered injury as a result of an "extraordinary rendition program" allegedly operated by the Central Intelligence Agency with logistical support from the defendant, Jeppesen Dataplan, Inc. *See id.* at 1073-75. In affirming dismissal of plaintiffs' claims, the Ninth Circuit concluded "that even assuming plaintiffs could establish their entire case solely through nonprivileged evidence – unlikely as that may be – any effort by Jeppesen to defend would unjustifiably risk disclosure of state secrets." *Id.* at 1090 (emphasis omitted); *see also id.* at 1088 (concluding that "*any* plausible effort by Jeppesen to defend against [plaintiffs' claims] would create an unjustifiable risk of revealing state secrets, even if plaintiffs could make a prima facie case on one or more claims with nonprivileged evidence").

The Fourth Circuit has affirmed dismissal of similar claims brought against government officials

and others whom the plaintiff alleged had unlawfully detained and interrogated him. *See El-Masri v. United States*, 479 F.3d 296, 299-300 (4th Cir. 2007). As one of the alternative holdings supporting affirmance, the court concluded that even if the plaintiff "were somehow able to make out a prima facie case despite the unavailability of state secrets, the defendants could not properly defend themselves without using privileged evidence" since "[t]he main avenues of defense available in this matter . . . would require disclosure of information" as to which the Government had invoked the state secrets privilege. *Id.* at 309; *cf. Farnsworth Cannon v. Grimes*, 635 F.2d 268, 276 (4th Cir. 1980) (en banc) (per curiam).

c. All of these cases are rooted in the principle that a court cannot grant affirmative relief when, as a result of the overriding necessity of holding the state secret inviolate, it cannot confidently conclude that such relief is warranted. In such cases, "the undisclosable scope of privilege lies so completely athwart the scope of proof relevant to resolution of the issues presented that litigation constrained by administration of the privilege simply could not afford the essential fairness of opportunity of both parties that is a fundamental assumption of the adversary system." *Id.* at 278 (Phillips, J., specially concurring in and dissenting from panel decision), *panel decision vacated on reh'g en banc*, 635 F.2d at 276.

In that circumstance – which the trial court found to be present in this case – "the right solution"

is to withhold adjudication of the claim. *Id.* at 279. Only by refusing to render judgment on the claim may the court assure itself that the blindness thrust upon it by the overriding necessity to protect the state secret has not led it to render a false or otherwise unjust judgment.

d. Proposed Federal Rule of Evidence 509, which would have codified the common-law state secrets privilege, likewise supports the principle that a government civil claim should be dismissed when the Government's assertion of the state secrets privilege substantially prejudices a private party's ability to defend. Although Congress ultimately rejected proposed Rule 509 and the twelve other originally proposed Federal Rules of Evidence relating to evidentiary privileges, they were "approved by the Judicial Conference of the United States and by this Court," *Jaffee v. Redmond,* 518 U.S. 1, 8 n.7 (1996), and the Court has found that they provide persuasive guidance. *See id.* at 14-15. As this Court recognized, Congress' rejection of the proposed Rules was motivated not by "disapprov[al]" of their substance but rather by "an affirmative intention not to freeze the law of privilege" in a code. *Id.* at 8-9 & n.7, 14-15 (quotation marks omitted); *Trammel v. United States*, 445 U.S. 40, 47 (1980).

Proposed Rule 509 would have codified the common-law state secrets privilege along the lines articulated in *Reynolds*. *See* Proposed Fed. R. Evid. 509(a)(1), (b), (c), 56 F.R.D. 183, 251-52 (1972); Advisory Committee's Notes to Proposed Rule 509(a)-(c),

id. at 252, 254. More pertinently, it also provided guidance for addressing the "[e]ffect of sustaining [a] claim" of state secrets privilege. Proposed Rule 509(e), *id.* at 252. Under proposed Rule 509, "[i]f [the state secrets] privilege [was] successfully claimed by the government in litigation to which it [was] *not* a party, the effect [was] simply to make the evidence unavailable, as though a witness had died or claimed the privilege against self-incrimination." Advisory Committee's Notes to Proposed Rule 509, *id.* at 254 (emphasis added). But if the government *was* a party to the proceeding and "it appear[ed] that another party [was] . . . deprived of material evidence" as a result of the Government's successful assertion of the privilege, proposed Rule 509 instructed the judge to "make any further orders which the interests of justice require[d], including striking the testimony of a witness, declaring a mistrial, finding against the government upon an issue as to which the evidence is relevant, or dismissing the action." Proposed Rule 509(e), *id.* at 252.

e. Well-established principles relating to judicial treatment of other evidentiary privileges further support a rule that a claim may not proceed when the Government's invocation of the state secrets privilege substantially prejudices a party's ability to defend against that claim. Particularly helpful guidance comes from "judicial experience" with the "analogous privilege . . . against self-incrimination." *Reynolds*, 345 U.S. at 7-8.

Courts have uniformly recognized that a defendant in a civil action should not be disadvantaged by the plaintiff's assertion of the Fifth Amendment privilege against self-incrimination. *See, e.g.*, *Wehling v. Columbia Broad. Sys.*, 608 F.2d 1084, 1088 (5th Cir. 1979). Consequently, in cases where "defendants would be substantially prejudiced" because "there [is] no effective substitute for" the withheld information and there is "no adequate alternative remedy" by which to prevent unfairness to the defendants, courts should dismiss the claim. *Serafino v. Hasbro, Inc.*, 82 F.3d 515, 518-19 (1st Cir. 1996); *cf. United States v. Rylander*, 460 U.S. 752, 758 (1983) ("We think the view of the Court of Appeals would convert the privilege from the shield against compulsory self-incrimination which it was intended to be into a sword whereby a claimant asserting the privilege would be freed from adducing proof in support of a burden which would otherwise have been his. None of our cases support this view.").

For example, in *Serafino* the plaintiff claimed that Hasbro and its CEO had retaliatorily "terminated certain business arrangements" but, invoking his privilege against self-incrimination, refused to answer deposition questions "concerning improprieties surrounding" those arrangements. 82 F.3d at 516-17. The withheld information was "central to defendants' defense" because, "if in fact the [arrangements] were illegally obtained," then the defendants could establish a "nonretaliatory reason for the termination." *Id.* at 518-19. "Without the ability to investigate a matter

that goes to the heart of the damages sought," the First Circuit said, "defendants would be substantially prejudiced" because "there was no effective substitute for" the withheld information. *Id.* at 518-19. Seeing "no adequate alternative remedy," the court affirmed dismissal. *Id.* at 519.

Similarly, in *Lyons v. Johnson*, the Ninth Circuit affirmed dismissal of civil rights claims brought by a plaintiff who invoked her Fifth Amendment privilege and refused to respond to any form of discovery concerning her claims. 415 F.2d 540, 541 (9th Cir. 1969). The court elaborated: "If any prejudice is to come from [the assertion of the privilege], it must, as a matter of basic fairness in the purposes and concepts on which the right of litigation rests, be to the party asserting the claim and not to the one who has been subjected to its assertion." *Id.* at 542; *see also Wehling*, 608 F.2d at 1087-88 (concluding that "it would be unfair" to require defendant "to defend against a party who refuses to reveal the very information which might absolve defendant of all liability"); *Afro-Lecon, Inc. v. United States*, 820 F.2d 1198, 1205-06 (Fed. Cir. 1987) (concluding that "a party may not claim a fifth amendment privilege and *proceed* with his suit").

The courts have applied a similar rule when addressing the attorney-client privilege, concluding that "where [the plaintiff's] assertion of a privilege results in the withholding of information necessary to [a] defense to [the] claim . . . , the privilege must give way to [the defendant's] right to mount a defense."

Ideal Elec. Sec. Co. v. International Fid. Ins. Co. ("IFIC"), 129 F.3d 143, 151 (D.C. Cir. 1997). As the D.C. Circuit explained, "Where society has subordinated its interest in the search for truth in favor of allowing certain information to remain confidential, it need not allow that confidentiality to be used as a tool for manipulation of the truth-seeking process." *Id.* at 151 (quotation marks omitted); *see also Greater Newburyport Clamshell Alliance v. Public Serv. Co.*, 838 F.2d 13, 20-22 (1st Cir. 1988) ("In a civil damages action, . . . fairness requires that the privilege holder surrender the privilege to the extent that it will weaken, in a meaningful way, the defendant's ability to defend."); *Conkling v. Turner*, 883 F.2d 431, 434-35 (5th Cir. 1989) (attorney-client privilege waived to extent necessary for defendant to establish affirmative defense). Although the result in these cases was waiver of the privilege rather than dismissal of the claim, these cases nevertheless show that a civil litigant cannot simultaneously maintain both its claim and its privilege in these circumstances.[13]

f. The Government itself has not hesitated to assert the foregoing principles when they serve its interests. Indeed, the Government has repeatedly,

[13] Of course, once the Government has properly invoked the state secrets privilege, a court-ordered waiver of the privilege is not permitted, leaving dismissal of the claim as the only option. *See Molerio*, 749 F.2d at 821 ("When properly invoked to protect such interests, the state secrets privilege is absolute. No competing public or private interest can be advanced to compel disclosure.") (quotation marks omitted).

aggressively, and (as the cases discussed above indicate) successfully argued that a private civil claim cannot proceed against the Government, its officials, or its contractors when the assertion of the state secrets privilege substantially prejudices the defense. *See, e.g.*, *Al-Haramain Islamic Found., Inc. v. Bush*, 507 F.3d 1190, 1197 (9th Cir. 2007); *Tenenbaum*, 372 F.3d at 777; *In re United States*, 872 F.2d at 477; *Molerio*, 749 F.2d at 819; *Hepting v. AT&T Corp.*, 439 F. Supp. 2d 974, 985-86 (N.D. Cal. 2006). Indeed, earlier *in this very case* the Government insisted that, if the court converted the termination for default to one for convenience, the Contractors' claim for an equitable adjustment and recovery of profits should nonetheless be denied because a potential government defense to that claim would depend upon privileged state secrets. Here is what the Government argued: "As a matter of law, 'if the privilege deprives the defendant of information that would otherwise give the defendant a valid defense to the claim, then the Court may grant summary judgment to the defendant.'" JA 1025 n.2 (quoting *Bareford*, 973 F.2d at 1141).

There is no principled reason why the rules that the Government so eagerly embraces when they serve its interests should not also apply when the shoe is on the Government's other foot. Certainly nothing in the decisions of this Court or the Courts of Appeals suggests that their holdings turn on the identity of the claimant. Furthermore, civil defendants subjected to government claims are entitled to at least the same

safeguards of due process and fundamental fairness that the Government claims for itself. Indeed, the fundamental purpose of due process protections is to safeguard against overreaching by the Government. "The purpose of an adversary hearing is to ensure the requisite neutrality that must inform all governmental decision-making. That protection is of particular importance here, where the Government has a direct pecuniary interest in the outcome of the proceeding." *United States v. James Daniel Good Real Prop.*, 510 U.S. 43, 55-56 (1993); *see also id.* at 56 ("It makes sense to scrutinize governmental action more closely when the State stands to benefit." (quoting *Harmelin v. Michigan*, 501 U.S. 957, 979 n.9 (1991) (opinion of Scalia, J.))).

* * *

In sum, a civil claim should be dismissed whenever application of the state secrets privilege substantially prejudices a litigant's ability to defend against the claim. Whatever the precise contours or outer limits of this rule, it plainly should apply in circumstances such as those presented here. In this case, as discussed above, the Government has asserted a punitive claim with severe potential consequences against the private Contractors.[14] The trial court

[14] Given the disparity between the private and government interests at stake, due process concerns have special force when the Government pursues a default termination claim against a private contractor *Cf. Matthews v. Eldridge*, 424 U.S. 319, 335 (1976) (balancing, *inter alia*, competing private and government

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found that the Contractors could present a prima facie valid superior knowledge defense based on the A-12 program information alone. *Supra* at 16-19, 22. But because the effect of the privileged evidence on the merits of that defense was "not readily apparent," Pet. App. 441a, and because litigating that defense would create an unacceptably high risk of disclosing the state secrets, *supra* at 15-20, 22-23; Pet. App. 246a, 376a, any ruling on the merits of the defense,

interests in determining due process requirements). As detailed above, *supra* at 9-11, such a claim can subject a private contractor to severe sanctions, including massive financial penalties, suspension, debarment, and unfavorable treatment in future government contracting. There can be no doubt that due process requires careful scrutiny of government action that threatens the imposition of such serious penalties. *See, e.g., Jones v Flowers*, 547 U.S. 220, 234, 239 (2006) (forfeiture); *James Daniel Good*, 510 U.S. at 55-56, 62 (same); *IMCO, Inc. v. United States*, 97 F.3d 1422, 1427 (Fed Cir. 1996) (contractor debarment); *Transco Sec., Inc. v. Freeman*, 639 F.2d 318, 321 (6th Cir. 1981) (same). The harshness of these sanctions contrasts sharply with the relatively mild consequences to the Government if it is barred from simultaneously pressing a default termination claim and ensuring its own victory by asserting the state secrets privilege. The result would simply be conversion of the default termination into a termination for the Government's convenience – a unique, government-friendly remedy unavailable to private contractors that allows the Government to terminate a contract at any time for essentially any reason without liability for breach-of-contract damages. *See supra* at 11-12. This result is far less severe than "letting the defendant go free," a result that due process and basic fairness require when the state secrets privilege prejudices a criminal defendant's ability to mount a defense to the charge. *Reynolds*, 345 U.S. at 12.

the trial court found, "would be a sham," Pet. App. 380a; *see supra* at 20, 22-23. The trial court and the appellate court thus barred the Contractors from pressing their prima facie valid superior knowledge defense. *See supra* at 19-20, 22-25; Pet. App. 207a-10a.

But it follows inexorably that proceeding without that defense rendered adjudication of the Government's default termination claim also "a sham," for a fair judgment on the Government's claim could not be reached with confidence when the Government's assertion of the state secrets privilege so substantially prejudiced the Contractors' ability to defend. Under these circumstances, the Government's default termination claim should not have been allowed to proceed, and the Federal Circuit's decision permitting the claim thus violates due process and fundamental principles of fairness.

♦

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be reversed, and the case should be remanded with instructions to convert the default termination to a termination for the convenience of the Government.

November 12, 2010

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RESPONDENT'S BRIEF

Nos. 09-1298 and 09-1302

In the Supreme Court of the United States

GENERAL DYNAMICS CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

THE BOEING COMPANY, SUCCESSOR TO MCDONNELL DOUGLAS CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

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QUESTION PRESENTED

Whether petitioners are entitled to a judgment vacating the agency decision that terminated their contract for default and awarding them money damages solely because the courts below concluded that the state-secrets privilege precluded adjudication of one of petitioners' claims seeking to excuse their default.

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BRIEF FOR THE UNITED STATES

STATEMENT

A. Factual Background

1. In the mid-1970s, petitioner General Dynamics Corporation (GD) developed an aircraft design concept that relied on "low observable" or "stealth" technologies to assist the aircraft in avoiding detection. J.A. 1240-1241, 1246-1255. GD marketed that design concept to the Air Force without success, eventually abandoning its

efforts in the early 1980s. J.A. 1241-1242, 1258-1259. In 1983, however, the Navy approached GD about the concept of a low-observable attack aircraft that could operate from an aircraft carrier. J.A. 1242, 1255-1257. In response, GD described the design that it had marketed to the Air Force as an "excellent candidate" for the Navy's needs. J.A. 1242.

In 1984, the Navy included GD in a select group of defense contractors that comprised Northrop Corporation (Northrop), which was then developing the B-2, a low-observable bomber aircraft for the Air Force; Lockheed Corporation (Lockheed), which had built the F-117A, a low-observable fighter aircraft for the Air Force; and McDonnell Douglas Corporation (MDC),[1] a builder of Navy carrier-based aircraft. The Navy invited those contractors to form teams among themselves, or with others in the industry, to compete for rights to develop and produce the new Navy low-observable attack jet, which became known as the A-12. Petitioners (GD and MDC) chose to collaborate to compete against a second team led by Northrop. J.A. 401-402.

In late 1984, the Navy awarded preliminary contracts to both teams to further explore their respective design concepts and attendant risks. Over the next few years, the Navy paid the competing teams to investigate appropriate technologies; to assist the Navy in drafting the technical specifications for the new aircraft; to assess and plan for technical, schedule, and cost risks associated with development; and to prepare a full-scale engineering development (FSED) contract proposal.

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[1] On January 1, 2010, MDC, which had been a wholly owned subsidiary of petitioner The Boeing Company (Boeing), was merged into Boeing. Because Boeing is now the corporate successor to MDC, this brief refers to MDC as a petitioner. GD Br. ii.

J.A. 402-403; see Pet. App. 43a & n.1. Aware that Northrop had held a "technical advantage in stealth" because of the B-2 and other experience, J.A. 1065, 1169-1171, GD entered into a subcontract with Lockheed after determining that Lockheed's support was "critical to the success of [a very low observable (VLO)] aircraft program," J.A. 1069. Throughout this period, "the Navy maintained the A-12 Program in a classified, special access status in which information concerning the A-12 was tightly controlled for national security purposes." J.A. 401; see Exec. Order No. 13,526, at § 4.3, 75 Fed. Reg. 707, 722-723 (2010) (authorizing special-access programs in "exceptional" circumstances).

In evaluating the FSED contract proposals, the Navy focused on the projected weight of each team's design because, *inter alia*, an aircraft's suitability for use on a carrier depends in part on its weight. The Navy warned petitioners that petitioners' projected weight for their design appeared to underestimate it by thousands of pounds. J.A. 1081-1085. Petitioners rejected the Navy's weight calculations and decided, largely for business reasons, to postpone a more accurate (and expensive) weight estimate until after the FSED contract was awarded. J.A. 1202-1205.

Price was another important factor in the Navy's choice of contractors. Contrary to petitioners' suggestion (GD Br. 4), the Navy did not attribute Northrop's higher bid for the FSED contract to its specialized knowledge from the B-2 program.[2] Rather, the Navy's

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[2] In support of its suggestion, GD quotes (Br. 4) from a Defense Department official's January 1988 memorandum, in which the official admits that she had only two hours to conduct her review and therefore could not offer a "firm, well-reasoned" opinion on A-12 contract pricing risks. J.A. 44. In any event, that memorandum observes that petition-

formal pre-award cost analysis concluded that the higher amount of Northrop's bid ($563 million, or about 12%, above petitioners' target price) was due largely to business factors such as estimated inflation rates and differing business arrangements within the respective teams, as well as bidding strategy. J.A. 1119-1123. Cognizant that winning the FSED contract could lead to a subsequent production contract for hundreds of aircraft, petitioners submitted an ambitious proposal to defeat the Northrop team's bid. In September 1987, petitioners made a new best and final fixed-price offer to "*confidently propose and accept a management challenge*," J.A. 1087, that reflected a price reduction of 7.5% from their "[e]stimated [c]ost" of performance, J.A. 1091. At the same time, petitioners proposed an "aggressive" 30-month schedule for flight of the first aircraft. J.A. 1088.

In their FSED contract proposal, petitioners represented to the Navy that they had identified and reduced significant risks and were prepared to proceed to the A-12 program's development phase. J.A. 1087. Petitioners did not make their proposal contingent on access to information from other classified (including special-access) programs. To the contrary, petitioners assured the Navy that they, together with their subcontractors, possessed "multi-company, real world experience" with low-observable technology. J.A. 1076-1078.

2. The Navy judged petitioners' contract proposal to be better than the Northrop team's proposal, and in January 1988 petitioners signed the FSED contract at a ceiling price of $4.8 billion. Pet. App. 2a. The contract required petitioners to, *inter alia*, complete a design that satisfied the technical specifications that they had

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ers "are strongly interested in becoming involved in stealth technology so they might be prepared to accept some risks to do so." J.A. 45.

helped to develop; manufacture all necessary tools and aircraft parts; assemble eight prototype aircraft in accordance with a delivery schedule petitioners had proposed; conduct ground-based and flight testing; support independent Navy testing; and prepare for transition to the program's production and deployment phases. *Id.* at 40a-51a.

The contract contained a progress-payment clause that required the government to advance funds to petitioners to finance the contract work. J.A. 111-124. Generally, under that clause, the government agreed to advance periodically a percentage of the costs petitioners had incurred by performing, so long as petitioners were making satisfactory progress, with the balance due upon satisfactory completion of the contract. J.A. 111-116. At petitioners' request, the contract also contained a special feature that entitled petitioners to receive final payment for certain contract work that was to be performed before delivery of the first aircraft. To implement that feature, the Navy agreed that it could accept such work, if satisfactory, as complete and thereby "liquidate" associated progress payments. J.A. 115-116; 48 C.F.R. 52.232-2 (1984); see C.A. App. 19,567 (incorporating clause into contract by reference); J.A. 49-51 (listing contract work items separately priced).

Because the A-12 program implicated sensitive, classified military technology, the FSED contract continued the strict special-access security requirements that had been put in place from the beginning of the program. The contract provided that contract work would be performed under the restrictions applicable to sensitive classified and special-access information, and it included detailed descriptions of all related security requirements. J.A. 73-76, 130-135, 150-202.

The contract also identified all technical information (J.A. 137-140), testing and evaluation equipment (J.A. 82-97, 141-149), and operating bases, laboratories, and other facilities (J.A. 97-107) that the government would make available to petitioners to support their performance of the contract. The contract established schedules specifying when the government would make available such information, equipment, and facilities. J.A. 100-104, 137-140. Nothing in the A-12 contract, however, entitled petitioners to receive access to classified, special-access information from other government programs not specified therein.

The FSED contract contained a standard clause allowing the government to terminate the contract for default if petitioners failed to satisfy the contract's terms or to make adequate progress. Pet. App. 2a-3a; 48 C.F.R. 52.249-9 (1984); see C.A. App. 19,576 (incorporating clause into contract by reference). The contract also specified that, if a default termination occurred, petitioners would return to the government any progress payments that had not been "liquidated" through government acceptance of completed, satisfactory work. J.A. 120-121. The contract further stated that, if a default termination occurred but it was later determined that petitioners were not actually in default or that their default was excused, the termination would be treated as one for the government's "convenience"—meaning without fault or breach by the contractors. J.A. 226. In that case, petitioners might be entitled to the costs of performance, profit on work performed, and expenses to close out their operations. 48 C.F.R. 52.249-2(f) (1984); see C.A. App. 19,576 (incorporating clause into contract by reference). If petitioners would have sustained a loss on the contract had it been completed, however, then any

termination-for-convenience recovery would be reduced to account for the rate of loss petitioners were experiencing at the time of termination. 48 C.F.R. 52.249-2(f)(2)(iii); see 48 C.F.R 49.203 (1984).

3. From the outset, petitioners encountered difficulties in designing and building an aircraft that would meet critical contract specifications within the negotiated schedule and ceiling price. In June 1988, less than six months after signing the FSED contract, petitioners had internally verified—consistent with the Navy's pre-award weight warning—that they had underestimated the weight of their design by several thousand pounds. J.A. 1097-1103.

In June 1990, petitioners failed to deliver the first aircraft as required under the contract. Pet. App. 4a. They informed the government that the cost of completing the contract work would substantially exceed the contract ceiling price, resulting in an estimated cost that petitioners viewed as "unacceptable." *Ibid.* Petitioners stated that "[o]ne of the fundamental causes for the present * * * situation on the A-12 program is the use of a fixed price type of contract for the [development] effort." J.A. 239-240. Petitioners proposed further negotiations to explore a fundamental restructuring of the contract. J.A. 239-243. At this point, petitioners did not claim that a current lack of access to other classified, compartmented programs was an impediment to their performance; rather, they expressed the need for more time and money and their desire to revise the contract's technical specifications.

Performance failures continued during the ensuing six months of negotiations. Petitioners failed to achieve

any of the delivery dates or program milestones originally established in the contract. Pet. App. 143a-144a.[3]

By December 1990, pursuant to the contract's progress-payment clause, the government had advanced petitioners approximately $2.7 billion, J.A. 326, one half of which was deemed "liquidated" in accordance with the special contract terms petitioners had negotiated, J.A. 339-340. That same month, the Navy issued a cure notice informing petitioners that their performance under the contract was "unsatisfactory" because of, *inter alia*, their failure to fabricate parts sufficient to meet the delivery schedule and their failure to meet specification requirements. Pet. App. 6a-7a. Because those deficiencies were "endangering performance of [the] contract," the Navy informed petitioners that it might terminate the contract for default. *Id.* at 7a.

In meetings with the government during the next two weeks, petitioners maintained that they could not build the A-12 aircraft for the price, schedule, and specifications that had been incorporated into the development contract. Pet. App. 7a; see J.A. 251-271, 279-312. Petitioners asserted they could not "get there if [they

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[3] In August 1990, because neither petitioner would commit to a schedule without first reaching agreement with the government on outstanding "technical and business" issues unrelated to sharing of government technology (Pet. App. 135a), the government unilaterally modified the contract to extend the delivery dates for all eight prototype aircraft by 18 to 25 months, thereby producing revised delivery dates ranging from December 1991 to February 1993. *Id.* at 5a, 199a-200a. At the time of the modification, petitioners stated that they believed they could deliver sooner than the revised schedule required. *Id.* at 225a. Several months later, however, petitioners projected a first delivery date of March 1992—a date in which petitioners themselves soon lost confidence, and which they believed to be achievable "only after significant changes." *Id.* at 5a-6a.

didn't] change the contract," and that the development contract had "to get reformed to a cost type contract or [they could not] do it." Pet. App. 7a (quoting J.A. 253, 261) (brackets in original). Petitioners submitted claims to the Navy seeking a $1.4 billion increase in the contract price. J.A. 396. In January 1991, in their formal response to the cure notice, petitioners reiterated that they would meet neither the contract's delivery schedules (original or revised) nor certain specifications. Pet. App. 7a; J.A. 272.

4. A few days later, the government terminated the contract for default. Pet. App. 8a; J.A. 313-318. The Navy's contracting officer notified petitioners that this action was based on petitioners' inability "to complete the design, development, fabrication, assembly and test of the A-12 aircraft within the contract schedule," as well as their "inability to deliver an aircraft that meets contract requirements." J.A. 314. Invoking the contract's default-termination clauses, J.A. 316-317, the contracting officer further advised petitioners (J.A. 315) that his letter was a final decision and apprised them of their appeal rights pursuant to the Contract Disputes Act of 1978 (CDA), 41 U.S.C. 601 *et seq.*[4]

By the time of contract termination, MDC's financial health had deteriorated to the point that the government agreed to defer recoupment of the unliquidated progress payments—totaling $1.35 billion—to avoid reducing one of its major contractors to a financial condition that

[4] Despite petitioners' insinuations of improper influence in the default-termination decision by the Defense Department under then-Secretary Cheney (GD Br. 5-6; Boeing Br. 5-6), the Federal Circuit decisions rejected petitioners' claim of procedural defects and upheld the determination that petitioners were in fact in default. Pet. App. 1a-34a, 250a-279a.

would endanger essential defense programs. J.A. 329-331, 342-348; see Pet. App. 8a. Although petitioners did not produce a single aircraft under the FSED contract, the government did not dispute that petitioners were entitled to retain the remaining $1.35 billion in progress payments, which had been liquidated pursuant to the contract.

B. Procedural History

1. In June 1991, petitioners filed suit in the Claims Court (now the Court of Federal Claims (CFC)), invoking the CDA, 41 U.S.C. 609(a)(1), and the Tucker Act, 28 U.S.C. 1491(a). J.A. 399. In a 20-count complaint, petitioners advanced an array of claims against the government. J.A. 437-476.

Some of those claims alleged that the FSED contract was void or voidable, resulting in an implied contract under which petitioners must be compensated, or was subject to an equitable adjustment in price and schedule. J.A. 437-442, 464. Almost all the other claims asserted either that petitioners were not in default or that their default was excused—*e.g.*, impossibility of performance, commercial impracticability, mutual mistake of fact, lack of enforceable delivery schedule, satisfactory progress, and defective default termination procedure. J.A. 442-464. As discussed below, all but one of the claims pressed by petitioners were ultimately rejected on the merits by the CFC or the Federal Circuit (or both). See pp. 14-17, *infra*. The remaining claim (Count IX) alleged that petitioners' performance delays and inability to achieve contract requirements were excusable by reason of the government's failure to disclose its "superior knowledge" of information vital to petitioners' performance. J.A. 452.

As affirmative relief, petitioners sought entry of a judgment, *inter alia*, holding that the Navy had breached the FSED contract; reforming the contract into a cost-reimbursement plus fixed-fee type contract; ordering the contracting officer to grant an equitable adjustment in the contract price; converting the termination for default into a termination for convenience; and awarding petitioners damages—including all their costs of performance, plus profit and settlement expenses—of approximately $4 billion plus interest. J.A. 473-475; see J.A. 397; Pet. App. 282a-283a.

2. Under the judge-made "superior knowledge" doctrine, the government is generally subject to an implied duty to share "vital knowledge" of a fact affecting a contractor's performance when it knows that the contractor is unaware of the information and not reasonably likely to obtain it. See *GAF Corp.* v. *United States*, 932 F.2d 947, 949 (Fed. Cir. 1991), cert. denied, 502 U.S. 1071 (1992); *Helene Curtis Indus., Inc.* v. *United States*, 312 F.2d 774, 778 (Ct. Cl. 1963). Petitioners alleged that under this implied duty, the Navy was obligated to disclose information that petitioners acknowledged was highly classified and "subject to extraordinary security and program access restrictions." J.A. 406; see J.A. 405-409, 451-452.

In 1992, the government moved to dismiss petitioners' superior-knowledge claim, arguing that the implied duty invoked by petitioners cannot be applied to require the government to disclose classified, special-access information. See Pet. App. 354a n.7. The CFC initially denied the motion, on the theory that the government had a duty to provide petitioners at least a "general warning" about potential production problems, and or-

dered discovery into other classified, special-access programs. *Ibid.*

Pursuant to the CFC's orders, the government permitted discovery into two classified, compartmented aircraft programs involving Northrop's B-2 bomber and Lockheed's F-117A fighter. Pet. App. 353a-355a. In March 1993, in response to a CFC order to provide additional classified, compartmented special-access information, the Acting Secretary of the Air Force invoked the state-secrets privilege to prevent disclosure of highly sensitive information. J.A. 516-523 (unclassified version).[5] In April 1995, after the Federal Circuit had granted two writs of mandamus overturning CFC discovery orders into classified information (J.A. 526-549, 552-575), the CFC terminated all discovery related to petitioners' superior-knowledge claim and bifurcated consideration of that claim from the rest of petitioners' claims. Pet. App. 355a; J.A. 795.

3. a. In December 1995, after a trial focusing on petitioners' claim that the default termination was procedurally defective (Count XVII, J.A. 463-464), the CFC set aside the default termination. Pet. App. 382a-429a. Although the CFC found that the contracting officer had "based the termination on the fault of the contractors because he did not believe that the Navy bore any responsibility for the contractors' perceived inability to achieve the contract specifications or deliver the aircraft on schedule," the court concluded that the termination

[5] The classified version of the March 1993 declaration by Acting Secretary of the Air Force Donley was placed on the docket of the CFC proceedings, see J.A. 11, and reviewed by the Federal Circuit, J.A. 556 n.2. Because of its classified nature, the declaration is stored with military security officials and will be made available to the Court upon request.

decision was not the product of "reasoned discretion." *Id.* at 402a, 407a. The CFC ordered that the termination be treated as one for the government's convenience, and it commenced damages proceedings. *Id.* at 382a-384a.

b. In December 1996, in conducting those proceedings, the CFC held that it would not consider petitioners' claim for profits or the government's position that the convenience-termination recovery must be reduced to reflect petitioners' projected contract losses. Pet. App. 343a-381a. After reviewing the classified declaration explaining the government's assertion of the state-secrets privilege, the CFC concluded that those issues were dependent upon petitioners' "superior knowledge" claim, which, it determined, could not be safely, fairly, or reliably litigated:

> We cannot permit the parties to litigate plaintiffs' [superior knowledge] claims for three reasons: (1) One party or the other would be unfairly prejudiced due to limitations placed on discovery by the Executive for national security reasons; (2) Highly classified information may be compromised in discovery despite procedures in place to prevent that from happening; and (3) Even if information available to the parties could be protected properly in discovery, other information necessary for the court to render an honest judgment would not be available.

Id. at 345a.

The CFC described the parties' competing positions on the merits of the "superior knowledge" claim, Pet. App. 353a-355a, 367a-370a, and concluded that "[j]ust as we acknowledge plaintiffs' belief that they could prove superior knowledge within the confines of the A-12 program, we know that the Government may have defenses

based on the factors described in *Helene Curtis Industries*," *id.* at 368a. The CFC noted, for example, that petitioners "are involved in other programs with the Government; it is possible that they did not lack knowledge about low-observable technology." *Ibid.* After noting certain security breaches that had occurred during the litigation, the CFC further found that information implicated by the superior-knowledge claim was highly vulnerable to inadvertent disclosure. *Id.* at 372a. Accordingly, the CFC concluded that "[d]espite everyone's best efforts, the risk of compromising national secrets is too serious to proceed to trial." *Id.* at 381a.[6]

The CFC ultimately ruled that petitioners were entitled to incurred costs of $3.9 billion, and it awarded petitioners a monetary judgment in the amount of $1.2 billion (net due after crediting $2.7 billion in progress payments already received by petitioners) plus interest. Pet. App. 341a-342a; J.A. 884-885. The government appealed the CFC's December 1995 liability ruling and its December 1996 damages ruling.

4. In 1999, the court of appeals reversed the CFC's judgment invalidating the default termination. Pet. App. 250a-279a. The Federal Circuit ruled that the CFC had "erred by vacating the termination for default without first determining whether a default existed." *Id.* at 269a. The court therefore remanded the case to the CFC to decide whether the default termination was justified. *Id.* at 278a.

Without expressing any view on the merits of the CFC's damages ruling, the Federal Circuit vacated that

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[6] In addition to its opinion, the CFC filed a "classified appendix" further addressing "the reasons for this ruling." Pet. App. 345a & n.2. The CFC directed that neither government nor petitioners' attorneys would be permitted access to that appendix.

ruling because, having reversed the CFC's liability decision, it viewed any question concerning the proper calculation of damages as unripe. Pet. App. 271a, 278a-279a. Noting the passage of time and other possible developments, the court invited the CFC to reconsider its state-secrets ruling pertaining to the superior-knowledge claim. *Id.* at 271a. This Court denied petitioners' petition for a writ of certiorari. 529 U.S. 1097 (2000).

5. On remand, petitioners served interrogatories pertaining to their superior-knowledge claim (see J.A. 971-972), and the Secretary of the Air Force again invoked the state-secrets privilege to prevent disclosure of highly sensitive information. J.A. 974-981 (unclassified version).[7] In 2001, after reviewing that second classified declaration, the CFC reaffirmed its prior ruling that petitioners' superior-knowledge claim could not be litigated because of national-security concerns, expressly adopting the state-secrets rationale from the vacated December 1996 ruling. Pet. App. 243a-246a. The CFC found that "the circumstances that prompted the [December 1996] ruling persist." *Id.* at 244a. The CFC stated that it was unable to "establish that the information that has been removed from this case would have benefitted either party. Without extensive discovery related to this information * * * no one can know whether either party would have been helped or hurt by it." *Id.* at 245a.

The CFC also sustained the default termination. Pet. App. 212a-249a. The CFC found that petitioners would not have delivered the first aircraft by the con-

[7] Secretary of the Air Force Peters's 2001 classified declaration was placed on the docket of the CFC proceedings. See J.A. 34. The declaration is stored with military security officials and will be made available to the Court upon request.

tractual deadline and therefore were in default of the contract. *Id.* at 218a-228a. The CFC rejected petitioners' various arguments for excusing their default, including their contentions that the revised delivery schedule was unreasonable and therefore unenforceable; that the schedule, even if enforceable, had been waived by the Navy; and that "the contract was impossible to perform." *Id.* at 228a-230a, 246a-248a.

The CFC entered judgment for the government, upholding the default termination and dismissing petitioners' complaint (including their superior-knowledge claim). J.A. 1262. In rejecting petitioners' post-trial motions to alter the judgment, the CFC reaffirmed its view that petitioners' allegations supporting their superior-knowledge claim "cannot be established."[8] J.A. 1264. Petitioners appealed.

6. In 2003, in its second published decision, the court of appeals affirmed in part and vacated in part. Pet. App. 178a-211a.

a. The Federal Circuit affirmed the CFC's dismissal of petitioners' superior-knowledge claim. Pet. App. 202a-210a. The court held that the government had properly invoked the state-secrets privilege and that the CFC had properly barred litigation of the superior-knowledge claim in light of the attendant risks. *Id.* at 205a-207a. The court also rejected petitioners' contention that, once the state-secrets privilege was found to preclude litigation of petitioners' superior-knowledge

[8] Petitioners nevertheless repeatedly state (*e.g.*, Boeing Br. 27-28; GD Br. 22) that the CFC found that they had established a prima facie "valid" claim of superior knowledge. As the CFC's ultimate 2001 ruling makes clear, however, it found that the validity of the claim could not be determined. J.A. 1264; see Pet. App. 245a ("*At one time* plaintiffs made a persuasive showing that they could prove their claim without the information.") (emphasis added).

claim, the Due Process Clause required the CFC to set aside the default termination. The Federal Circuit relied on this Court's distinction in *United States* v. *Reynolds*, 345 U.S. 1, 12 (1953), between the government as criminal prosecutor and the government as civil defendant. The court explained that, like the plaintiff in *Reynolds*, petitioners "are the plaintiffs in this purely civil matter, suing the sovereign on the limited terms to which it has consented." Pet. App. 208a.

b. The Federal Circuit affirmed the CFC's ruling that the contract delivery schedule was enforceable and had not been waived, Pet. App. 198a-202a, but held that the CFC "did not make adequate findings" to sustain the default termination. *Id.* at 187a. The court remanded the case to the CFC. *Id.* at 196a-197a.

7. a. In 2007, the CFC again sustained the default termination, Pet. App. 35a-177a, concluding that the government was justified in terminating the contract for petitioners' failure to make progress, *id.* at 133a-155a. The CFC entered judgment in favor of the government, and petitioners appealed again.

b. In 2009, in its third published decision, the court of appeals affirmed. Pet. App. 1a-34a. Based on its review of the record, the Federal Circuit held that the government had satisfied its burden under *Lisbon Contractors, Inc.* v. *United States*, 828 F.2d 759 (1987), of establishing a reasonable belief that there was no reasonable likelihood of timely performance of the contract. Pet. App. 22a-27a. Petitioners did not raise, and the Federal Circuit did not address, the superior-knowledge claim in that 2009 appeal.

8. This Court granted certiorari limited to the question whether the default termination should have been set aside because the government's invocation of the

state-secrets privilege prevented judicial resolution of petitioners' superior-knowledge claim. See 131 S. Ct. 62 (2010).

SUMMARY OF ARGUMENT

A. The state-secrets privilege serves the singularly compelling purpose of protecting national security. For at least a half century, it has been settled law that while the government may not criminally prosecute a defendant while invoking the state-secrets privilege to bar a defense, it cannot be penalized for invoking the privilege "in a civil forum where the Government is not the moving party, but is a defendant only on terms to which it has consented." *United States* v. *Reynolds*, 345 U.S. 1, 12 (1953). Subjecting the government to liability in such cases would improperly interfere with the Executive's decision to invoke the state-secrets privilege; it would encourage private parties to raise marginal or meritless claims to induce the privilege's invocation; and it would prejudice the public fisc by allowing money judgments against the government on claims that have not been proved.

B. Petitioners, who filed this lawsuit in 1991, are obviously the "moving parties" in this civil case. Pursuant to the limited waivers of sovereign immunity in the Tucker Act, 28 U.S.C. 1491(a), and the CDA, 41 U.S.C. 609(a)(1), petitioners brought suit against the government in the CFC to challenge the default termination of the A-12 contract. Petitioners sought vacatur of the contracting officer's decision and more than a billion dollars in additional government funds, while the government sought no affirmative relief whatsoever from the CFC. And while the government bears the burden of proof on the issue of default, the government carried that burden here.

The information as to which the government invoked the state-secrets privilege is potentially relevant solely to petitioners' superior-knowledge claim, on which petitioners, not the government, bore the burden of proof. Neither precedent nor logic supports petitioners' contention that the courts below were required to dispose of this case as though petitioners had proved their superior-knowledge claim and to order affirmative relief against the government based on that counter-factual hypothesis, even though the government's appropriate invocation of the state-secrets privilege made actual resolution of that claim impossible. The fact that the government is entitled to return of *unliquidated* progress payments as a result of the default termination—a happenstance of the timing of payments under the A-12 contract—does not change the analysis.

C. Even if the government were deemed the "moving party" in this case, the Federal Circuit's judgment should be affirmed. Although *Reynolds* did not discuss the proper disposition of civil cases in which the government as plaintiff invokes the state-secrets privilege, it would be inappropriate to extend to this civil case the rule noted in *Reynolds* that the government as criminal prosecutor cannot invoke the state-secrets privilege and foreclose the defendant from litigating a potentially viable defense. No court in a civil case has ever entered judgment against the government in response to the government's proper invocation of the state-secrets privilege. Courts have similarly refused to dismiss the claims of civil plaintiffs even for the invocation of other privileges that do not implicate the Nation's security.

D. Contrary to petitioners' suggestion, there is no reason to believe that federal officials will improperly invoke the state-secrets privilege in similar future litiga-

tion, to the detriment of defense contracting, if the Federal Circuit's decision is affirmed. The safeguards against capricious invocation of the privilege lie in the procedural and substantive restrictions that this Court imposed in *Reynolds*, 345 U.S. at 7-8, and in the presumption that agency heads discharge their duties in good faith—not in any judicially fashioned prophylactic rule that the government loses claims as to which the privilege has been invoked. The government has a strong interest in attracting capable defense contractors, who are sophisticated enough to use market-based solutions to protect themselves against any perceived risk in their negotiation of future contracts. Under petitioners' proposed rule, by contrast, contractors could raise marginal or meritless superior-knowledge or other claims simply to induce the government to invoke the state-secrets privilege, thereby achieving automatic invalidation of a justified default termination.

E. If this Court holds that the courts below improperly granted judgment in the government's favor, the Court should remand for consideration of additional defenses that the government preserved concerning the superior-knowledge claim. Those threshold legal defenses were pressed but never passed on in the Federal Circuit, and they do not require resort to privileged information. In any event, contrary to petitioner GD's contention, reinstatement of the CFC's 1998 damages award is not warranted. The Federal Circuit never ruled on the government's challenge to that $1.2 billion (plus interest) award on the merits because the court vacated the flawed award as moot in 1999.

ARGUMENT

AFTER DETERMINING THAT PETITIONERS WERE IN DEFAULT, AND THAT FURTHER LITIGATION OF PETITIONERS' SUPERIOR-KNOWLEDGE CLAIM RISKED THE DISCLOSURE OF STATE SECRETS, THE COURTS BELOW CORRECTLY ENTERED JUDGMENT FOR THE GOVERNMENT

Petitioners brought this suit to challenge the termination for default of the FSED contract. After nearly two decades of litigation, including multiple trials and appeals, the courts below rejected on the merits all the claims pressed by petitioners except for their superior-knowledge claim. The courts below concluded, and petitioners do not dispute, that the state-secrets privilege was properly invoked in this case and that their superior-knowledge claim could not be litigated without risking disclosure of military and state secrets. GD Br. 35-36, 50; Boeing Br. 27, 33.

Petitioners contend, however, that the necessary consequences of the government's unchallenged invocation of the state-secrets privilege were entry of judgment against the United States, invalidation of the contracting officer's default termination, and a gigantic monetary award in petitioners' favor. Regardless of how this case is ultimately resolved, petitioners will retain $1.35 billion in *liquidated* progress payments, of which the government has never sought return. Under petitioners' theory, petitioners would keep another $1.35 billion in *unliquidated* progress payments (the return of which would be required under a default termination) and would receive an additional $1.2 billion (plus interest) in damages.

In petitioners' view, the government's unchallenged invocation of the state-secrets privilege compels those results even though the courts below held that petition-

ers were in default of the contract, the superior-knowledge issue to which the privileged information pertained was one on which petitioners bore the burden of proof, and the government did not receive a single aircraft. Petitioners thus contend that the courts below were required to dispose of this case *as though* petitioners had carried their burden of proof on their superior-knowledge claim, and to enter affirmative relief against the United States on that basis, even though the government's appropriate invocation of the state-secrets privilege made actual resolution of that claim impossible. No decision of this Court or any court of appeals supports the view that the government should be penalized in that manner for safeguarding vital national-security information.

A. Penalizing The Government For Its Invocation Of The State-Secrets Privilege Would Undermine The Privilege's Paramount Purpose Of Protecting National Security

1. The long-recognized purpose of the state-secrets privilege is to protect national security

From the earliest days of the Republic, courts have recognized the need to protect information critical to national security. See *United States* v. *Burr*, 25 F. Cas. 30, 37 (C.C. Va. 1807); *Martin* v. *Mott*, 25 U.S. 19, 31 (1827). This Court's first two detailed discussions of the state-secrets doctrine—*Totten* v. *United States*, 92 U.S. 105, 107 (1875) (barring suit that might expose confidential information "to the serious detriment of the public"), and *United States* v. *Reynolds*, 345 U.S. 1, 10 (1953) (permitting government to withhold evidence concerning "military matters" "in the interest of national security") —recognize the importance of the state-secrets doctrine

to the protection of national security, an interest this Court has repeatedly deemed "compelling." *Department of the Navy* v. *Egan*, 484 U.S. 518, 527 (1988). Indeed, the Court has found it "'obvious and unarguable' that no governmental interest is more compelling than the security of the Nation." *Haig* v. *Agee*, 453 U.S. 280, 307 (1981). The responsibility to protect national-security information "falls on the President as head of the Executive Branch and as Commander in Chief." *Egan*, 484 U.S. at 527. The state-secrets privilege is deeply rooted in "the law of evidence," *Reynolds*, 345 U.S. at 6-7, and reflects the Executive's constitutional duty to protect "military or diplomatic secrets," *United States* v. *Nixon*, 418 U.S. 683, 710 (1974).

2. The standards for and consequences of invoking the state-secrets privilege are well established and critical to its proper and effective use

a. The basic rules governing the assertion of the state-secrets privilege are well established and not in dispute here. The privilege "belongs to the Government," which must assert it in a "formal claim of privilege, lodged by the head of the department which has control over the matter, after actual personal consideration by that officer." *Reynolds*, 345 U.S. at 7-8 (footnotes omitted). The state-secrets privilege applies when "there is a reasonable danger that compulsion of the evidence will expose military matters which, in the interest of national security, should not be divulged." *Id.* at 10. Although "[t]he court itself must determine whether the circumstances are appropriate for the claim of privilege," it must not in the course of considering that claim "forc[e] a disclosure of the very thing the privilege is designed to protect." *Id.* at 8. When properly invoked, the privilege is absolute: "even the most compelling

necessity cannot overcome the claim of privilege if the court is ultimately satisfied that military secrets are at stake." *Id.* at 11.

b. When a court sustains a claim of privilege, it must then determine how, if at all, the litigation should move forward. Litigation generally should proceed if the privileged information is not necessary to litigate the claims and further litigation would not risk disclosure of state secrets. In *Reynolds*, for example, private parties brought a tort suit against the government arising out of a military plane crash and sought discovery of an accident-investigaton report, which the government withheld on the ground that it implicated military secrets. 345 U.S. at 2-4. In reversing the trial court's judgment against the government, this Court remanded for further proceedings to determine whether it was "possible for [the plaintiffs] to adduce the essential facts as to causation without resort to material touching upon military secrets." *Id.* at 11.

In other cases involving state secrets, however, further litigation may not be possible. This Court has recognized on several occasions that when a claim against the government cannot be litigated because it would risk disclosure of state secrets, the claim must be dismissed altogether. "[P]ublic policy forbids the maintenance of any suit in a court of justice, the trial of which would inevitably lead to the disclosure of matters which the law itself regards as confidential." *Totten*, 92 U.S. at 107; see *Tenet* v. *Doe*, 544 U.S. 1, 8 (2005); *Weinberger* v. *Catholic Action of Haw./Peace Educ. Project*, 454 U.S. 139, 146-147 (1981).

The Court in *Reynolds* identified one circumstance in which the government's proper invocation of the state-secrets privilege will result in dismissal of the gov-

ernment's case. The Court noted that, in federal criminal cases, lower courts had held that "the Government can invoke its evidentiary privileges only at the price of letting the defendant go free." *Reynolds*, 345 U.S. at 12 (footnote omitted). The Court explained that "[t]he rationale of the criminal cases is that, since the Government which prosecutes an accused also has the duty to see that justice is done, it is unconscionable to allow it to undertake prosecution and then invoke its governmental privileges to deprive the accused of anything which might be material to his defense." *Ibid.* The Court further held, however, that "[s]uch rationale has no application in a civil forum where the Government is not the moving party, but is a defendant only on terms to which it has consented." *Ibid.*

Applying the guidance from *Reynolds*, the courts of appeals uniformly have held that a private party whose claim cannot be adjudicated because its litigation would threaten national security cannot be awarded affirmative relief. Instead, the claim is dismissed without any adverse litigation consequence to the government. See, *e.g.*, *El-Masri* v. *United States*, 479 F.3d 296, 313 (4th Cir.) (dismissing claims of unlawful detention and interrogation because "privileged state secrets are sufficiently central to the matter"), cert. denied, 552 U.S. 947 (2007); *Sterling* v. *Tenet*, 416 F.3d 338, 348 (4th Cir. 2005) (dismissing Title VII discrimination claim by former CIA employee because it could not be litigated "without presenting evidence on topics that are state secrets"), cert. denied, 546 U.S. 1093 (2006); *Tenenbaum* v. *Simonini*, 372 F.3d 776, 777 (6th Cir.) (dismissing religious-discrimination claims against federal agency personnel because "a reasonable danger exists that disclosing the information in court proceedings would harm

national security interests"), cert. denied, 543 U.S. 1000 (2004); *Black* v. *United States*, 62 F.3d 1115, 1119 (8th Cir. 1995) (dismissing tort claims because "litigation cannot be tailored to accommodate the loss of the [state-secrets] privileged information").

c. *Reynolds* and the uniform body of case law applying it reflect a recognition that the state-secrets privilege will not serve its vital purposes if the automatic consequence of invoking it is entry of judgment against the government. Even if no evidentiary privilege were available, the government could refuse to produce secret material (or abstain from litigating the claim altogether) and risk a default judgment. That is precisely the dilemma to which this Court in *Reynolds* refused to put the government. See 345 U.S. at 5 (reversing trial court's sanctions order under Federal Rule of Civil Procedure 37(b)(2)(i) "that the facts on the issue of negligence would be taken as established in plaintiffs' favor").

Moreover, if the government's proper invocation of the state-secrets privilege could result in a substantial monetary award against the United States, the duty of high-level Executive Branch officials to safeguard national security would come into conflict with their responsibility to protect the public fisc. Although those officials presumably would give precedence to their national-security obligations, the courts should not create such disincentives to appropriate invocation of the state-secrets privilege.

In addition, if judgment in the plaintiff's favor were required whenever invocation of the privilege made it impossible to litigate the plaintiff's claim, private litigants would be encouraged to raise marginal or meritless claims that potentially implicate secret infor-

mation, with the hope of inducing an invocation of the state-secrets privilege. Cf. *Tenet*, 544 U.S. at 11 ("Forcing the Government to litigate these claims would * * * make it vulnerable to 'graymail,' *i.e.*, individual lawsuits brought to induce the [government] to settle a case (or prevent its filing) out of fear that any effort to litigate the action would reveal classified information."). For all these reasons, the government should not be "punished for asserting the [state-secrets] privilege." *Salisbury* v. *United States*, 690 F.2d 966, 975 (D.C. Cir. 1982); see *id.* at 976 (observing that "[o]ther courts have also refused to employ sanctions against the United States for exercise of its state secrets privilege").

B. The Government Is Not The "Moving Party," Either Procedurally Or Substantively, In This Civil Case

As just discussed, *Reynolds* unequivocally holds—and petitioners do not dispute—that subjecting the government to an adverse judgment in response to a proper invocation of the state-secrets privilege is improper "in a civil forum where the Government is not the moving party, but is a defendant only on terms to which it has consented." 345 U.S. at 12. Petitioners contend (GD Br. 3, 40) that, despite filing a lawsuit seeking affirmative monetary relief against the government, they are merely "nominal plaintiffs" and not the "moving party." That contention lacks merit.

1. Petitioners are the "moving party" here because they brought this suit seeking affirmative relief against the government

a. In *Reynolds*, the private plaintiffs sued the government pursuant to the waiver of sovereign immunity effected by the Federal Tort Claims Act. 345 U.S. at 6.

By contrasting the term "moving party" with "a defendant only on terms to which it has consented," the *Reynolds* Court indicated that the government is not a "moving party" when a suit is brought against it pursuant to a limited waiver of sovereign immunity. *Id.* at 12. Under that formulation, the government is not a "moving party" here, since petitioners sued the government in the CFC pursuant to the limited waiver of sovereign immunity effected by the Tucker Act and the CDA. See 28 U.S.C 1491(a)(1); 41 U.S.C. 605(a), 609(a)(1). Indeed, because the CFC's jurisdiction is limited to suits against the United States (28 U.S.C. 1491), the government could not have been a plaintiff in that court.

b. Even if the term "moving party" as used in *Reynolds* could encompass some defendants (*e.g.*, those who file counterclaims against the plaintiff), it at least requires that the party seek affirmative judicial relief against another party. In this case, petitioners were the only parties seeking affirmative relief from the CFC.

Petitioners' complaint requests various forms of equitable relief as well as substantial money damages. J.A. 473-475. In this Court, GD seeks reinstatement of the original money judgment petitioners received from the CFC in 1998. GD Br. 58-61. Based on its conversion of the default termination to a termination for convenience (later overturned by the Federal Circuit), the CFC calculated petitioners' costs incurred to be $3.9 billion. Pet. App. 341a-342a. Because petitioners already possessed $2.7 billion in progress payments from the government (of which $1.35 billion was unliquidated), the CFC initially entered judgment against the government for an additional $1.2 billion plus interest. J.A. 884-885. It defies not only *Reynolds* but also common sense to contend that a plaintiff that seeks a judg-

ment setting aside the decision of a federal administrative official (here, the contracting officer), and ordering the government to pay more than a billion dollars to the plaintiff, is not the "moving party" in its own lawsuit.

By contrast, the government sought no affirmative relief from the CFC. Indeed, when the CFC ultimately rendered judgment in favor of the government after the government had proved petitioners' default at trial, the court's order stated simply that petitioners' "complaint was dismissed." J.A. 1262; see J.A. 1264 (post-trial order noting that the CFC did not "enter a money judgment for the United States"). The CFC's final judgment, which was wholly favorable to the government, thus produced exactly the same practical result as if the suit had never been filed.

c. The fact that the suit was commenced in response to a contracting officer's administrative decision does not detract from petitioners' status as plaintiffs or "moving parties" in the judicial proceedings. Almost every lawsuit against the government can be characterized as a reaction to some government official's action. Persons who challenge adverse agency action are treated as plaintiffs and must identify an applicable waiver of sovereign immunity. When the government has invoked the state-secrets privilege in response to such suits, and the plaintiffs' claims (including those alleging a violation of constitutional rights) are no longer justiciable as a result, the courts of appeals have uniformly dismissed the suits. See, *e.g.*, *Sterling*, 416 F.3d at 348-349 (affirming dismissal of former CIA employee's Title VII action); *Kasza* v. *Browner*, 133 F.3d 1159, 1168-1170 (9th Cir.) (affirming dismissal of suit against Air Force under the Resource Conservation and Recovery Act of 1976, 42 U.S.C. 6972, alleging noncompliance with hazardous-

waste inventory and reporting requirements), cert. denied, 525 U.S. 967 (1998); see also *Edmonds* v. *Department of Justice*, 161 Fed. Appx. 6 (D.C. Cir. 2005) (affirming dismissal of claims by former FBI employee alleging under the Administrative Procedures Act that FBI's termination of her employment violated various statutory and constitutional provisions), aff'g 323 F. Supp. 2d 65 (D.D.C. 2004); cf. *Weinberger*, 454 U.S. at 146-147 (analogizing to *Totten* and *Reynolds* in holding that question "whether or not the Navy has complied with [the National Environmental Policy Act of 1969] 'to the fullest extent possible' is beyond judicial scrutiny" where plaintiff's challenge implicated national-security information).

Petitioners identify no case in which a court has treated the government's invocation of the state-secrets privilege during judicial-review proceedings as a ground for setting aside the administrative action that was the subject of the plaintiff's suit. There is no sound reason for ordering that relief here. That is particularly so because petitioners (unlike most of the complainants in the above-cited cases) were able fully to litigate (albeit unsuccessfully) their claim that they were not actually in default of their contractual obligations.

2. Neither the characterization of default termination as a "government claim" under the CDA, nor the fact that the government bore the burden of proof on the issue of default, makes the government the "moving party" in this judicial proceeding

Petitioners' characterization of the government as the "moving party" in this case is based in significant part on Federal Circuit decisions describing default termination as a "government claim" for which the govern-

ment bears the burden of proof under the CDA. GD Br. 41-45; Boeing Br. 37-39. Neither that label nor the applicable burden of proof alters the conclusion that petitioners are the "moving party" here.

a. Congress enacted the CDA, which applies generally to contracts involving the government's acquisition of goods or services, to "provide[] a fair, balanced, and comprehensive statutory system of legal and administrative remedies in resolving Government contract claims." S. Rep. No. 1118, 95th Cong., 2d Sess. 1 (1978). The CDA contemplates government "claims" in proceedings before the contracting officer. 41 U.S.C. 605(a) ("All claims by the government against a contractor relating to a contract shall be the subject of a decision by the contracting officer."). The Federal Circuit has held that the government's termination of a contract for default is a government "claim" in those administrative proceedings. *Lisbon Contractors, Inc.* v. *United States*, 828 F.2d 759, 765 (1987); see *Malone* v. *United States*, 849 F.2d 1441, 1443 (1988) ("A default termination falls precisely within the contours of" 41 U.S.C. 605(a).).

Although the CDA authorizes the government to assert a claim through issuance of a contracting officer's final decision, the government has no similar right to commence a suit in the CFC. Once a contracting officer terminates a contract for default, that decision stands as "final and conclusive," 41 U.S.C. 605(b), unless the contractor either pursues an appeal to the agency's board of contract appeals, 41 U.S.C. 607, or files a lawsuit in the CFC, 41 U.S.C. 609(a)(1). Because only the contractor can file suit in the CFC, the statutory scheme does not provide for "government claims" in that court. Petitioners rely (GD Br. 43; Boeing Br. 9, 39) on the Federal Circuit's statement in *Lisbon* that the burden of estab-

lishing a contractor's default rests with the government in judicial as well as administrative proceedings. The court in *Lisbon* reasoned that "the government is only being made to bear the burden of proof on its own 'claim' of default." 828 F.2d at 764. The Federal Circuit's use of that terminology, however, cannot alter the fact that petitioners were the only parties entitled by statute to invoke the CFC's jurisdiction in this case, and the only parties who requested any affirmative relief from that court.

b. Petitioners are the "moving party" not only with respect to the suit as a whole, but also with respect to the specific issue to which the privileged information is potentially relevant. When a private contractor files suit in the CFC to challenge a default termination, the government bears the burden of proof on the question whether a default occurred. See *Lisbon*, 828 F.2d at 763 ("We conclude that the government bears the burden of proof on the *issue* of default by the contractor in this type of proceeding."). In a case like this one, the government therefore must establish that the contractor was failing to "[p]rosecute the work so as to endanger performance of this contract." 48 C.F.R. 52.249-9(a)(1)(ii).[9] Here, after multiple trials and appeals, the courts below concluded that the government had satisfied that burden, see Pet. App. 33a, and the government's invocation of the state-secrets privilege did not affect that determination.

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[9] Petitioners are incorrect in asserting that the filing in the CFC of a lawsuit challenging a default termination "effectively vacat[es]" the underlying default termination decision. GD Br. 2, 43. The default termination remains in force pending *de novo* judicial review, and the contracting officer's decision becomes conclusive unless the challenge succeeds, just as if there had been no challenge at all. 41 U.S.C. 605(b).

The evidence that was rendered unavailable by the government's invocation of the state-secrets privilege was at most potentially relevant, not to the question whether petitioners were in default, but to petitioners' contention that their default was excusable because the government allegedly failed to share its "superior knowledge." As explained above (see pp. 31-32, *supra*), a plaintiff who commences suit in court and seeks affirmative judicial relief is properly viewed as the "moving party" under *Reynolds*, even if the government bears the burden of proof on some subsidiary questions. But even if it were appropriate to identify the "moving party" by fracturing the various issues involved in a lawsuit and focusing on the one to which state-secrets information is potentially relevant, petitioners would be the "moving party" with respect to their superior-knowledge claim. The gravamen of the superior-knowledge claim is that the government breached an implied duty under the contract; petitioners bore the burden of proving that such a breach occurred and that it excused their own failure to perform. See *GAF Corp.* v. *United States*, 932 F.2d 947, 949 (Fed. Cir. 1991); *Daewoo Eng'g and Constr. Co.* v. *United States*, 73 Fed. Cl. 547, 564 (2006), aff'd, 557 F.3d 1332 (Fed. Cir.), cert. denied, 130 S. Ct. 490 (2009); see also, *e.g.*, *DCX, Inc.* v. *Perry*, 79 F.3d 132, 134 (Fed. Cir.), cert. denied, 519 U.S. 992 (1996); 13 Richard A. Lord, *Williston on Contracts* § 39.1, at 511-512 (4th ed. 2000) (*Williston*). Petitioners identify no plausible reason for treating the government as the "moving party" in this case simply because the government bore (and satisfied) the burden of proof on a dis-

tinct issue (the occurrence of a default) to which the privileged information was irrelevant.[10]

In both *Tenet* and *Totten*, this Court held that the imperatives of national security foreclosed the lower courts from determining whether the government had in fact breached contractual obligations to the plaintiffs. The Court then resolved both cases, not by awarding the plaintiffs the relief to which they would have been entitled if they had proved that breaches of contract occurred, but by ordering that the suits be dismissed. See *Tenet*, 544 U.S. at 8-11; *Totten*, 92 U.S. at 105-107. Petitioners' contention that the government's alleged breach of duty to share its "superior knowledge" should be treated as proved cannot be reconciled with those dispositions. To be sure, petitioners' superior-knowledge claim is simply one aspect of a wide-ranging complaint, whereas the contract claims that the Court found nonjusticiable in *Tenet* and *Totten* were the entirety of the suits. The fact that petitioners were allowed to litigate a multitude of other claims, however, makes the impact on them less, rather than more, severe.

Petitioners contend that, "[w]hen the just outcome is unknowable, a court must refrain from exercising its power in the claimant's favor, not take affirmative action that might very well be wrong." GD Br. 23; see *id.* at 31;

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[10] Petitioners also contend that the contract's disputes clause, which incorporated the relevant provisions of the CDA, "assur[ed] them the opportunity to require the government to prove any default claim, subject to their defenses," GD Br. 45, and that the removal of their superior-knowledge claim "deprived the Contractors of the process to which they—and the government—agreed," *id.* at 46. Nothing in the disputes clause (or in any other provision of the contract or the CDA), however, guaranteed petitioners the right to adjudication of claims rendered nonjusticiable by a proper assertion of the state-secrets privilege.

Boeing Br. 30-31. Any concern about active judicial participation in a possible injustice, however, weighs entirely in favor of the government. Petitioners, not the government, invoked the jurisdiction of the CFC. They sought vacatur of the contracting officer's decision and asked for a court order directing the United States to pay them more than a billion dollars in additional funds, whereas the United States simply urged dismissal of the suit. Petitioners further contend that the CFC should have decided this case as though their superior-knowledge claim had been established, even though petitioners bore the burden of proof on that issue and all parties agree that petitioners did not actually carry that burden. It is thus petitioners, not the government, that urged the courts below to "take affirmative action that might very well be wrong."

In addition, the *Reynolds* Court's reference to the United States as "a defendant only on terms to which it has consented," 345 U.S. at 6, reflects the principle that "the United States, as sovereign 'is immune from suit save as it consents to be sued,'" *United States* v. *Testan*, 424 U.S. 392, 399 (1976) (quoting *United States* v. *Sherwood*, 312 U.S. 584, 586 (1941)). Although Congress has authorized the CFC to award monetary relief to a plaintiff that establishes the government's breach of contract, the United States "has never consented to an *increase* in its exposure to liability when it is compelled, for reasons of national security, to refuse to release relevant evidence." *Ellsberg* v. *Mitchell*, 709 F.2d 51, 64 (D.C. Cir. 1983), cert. denied, 465 U.S. 1038 (1984); cf. Fed. R. Civ. P. 55(d) (permitting default judgment against the government "only if the claimant establishes a claim or right to relief by evidence that satisfies the court"). Because the "waiver of the Government's sover-

eign immunity will be strictly construed, in terms of its scope, in favor of the sovereign," *Lane* v. *Pena*, 518 U.S. 187, 192 (1996), it would be particularly inappropriate, absent clear congressional authorization of such a step, for a court to treat the government's assertion of the state-secrets privilege as a ground for ordering the United States to pay money on a claim the plaintiff has not proved.

c. Contrary to Boeing's contention (Br. 38), their status as the "moving party" in this suit is not "simply an artifact" of the "Government-friendly" CDA.[11] The government here is similarly situated to a private defendant who is sued for breach of contract after terminating a contract because of the other party's failure to perform. In those circumstances, both private and governmental defendants bear the burden of justifying the termination based on the plaintiff's nonperformance, see 2 E. Allan Farnsworth, *Farnsworth on Contracts* § 8.15, at 509 (3d ed. 2004); 13 *Williston* § 39.1, at 511-512, but the plaintiff who commences the suit and seeks judicial relief is still the "moving party" in the litigation.

The fact that the contracting officer's default termination gave rise to a right to return of unliquidated progress payments does not mean that the government was the "moving party" in the lawsuit or that it sought relief *in court*. Had the first progress payment required by the A-12 contract not come due before the date that the government determined that petitioners were in default, the government could have declined to make the

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[11] GD (Br. 49) evidently disagrees with Boeing's characterization of the CDA. In any event, as explained below (pp. 51-52, *infra*), petitioners voluntarily agreed to the FSED contract under the CDA framework, and so any "Government-friendly" terms in it do not help petitioners.

progress payment (or any other payments). Alternatively, once the contracting officer's decision had established the existence of a debt to the United States in the amount of the unliquidated progress payments, the government could have sought to recoup the funds by offsetting that amount against payments owed petitioners under other contracts. Cf. *Astrue* v. *Ratliff*, 130 S. Ct. 2521 (2010). In either scenario, petitioners would then have been forced to bring suit in the CFC against the government. In such lawsuits, petitioners clearly would have been plaintiffs (and "moving parties") and the government the defendant—free to raise petitioners' nonperformance as a defense. The consequence of invoking the state-secrets privilege should be no different in this case.

3. The default termination in this case imposes no punitive consequences

Seeking to avail themselves of decisions requiring the government to forgo criminal prosecution when it invokes certain privileges, petitioners characterize the potential consequences of a default termination as quasi-criminal or punitive in nature. GD Br. 2, 44-45, 54; Boeing Br. 9-11, 24, 28, 36-37, 42. That characterization is plainly wrong on the facts of this case (and, as explained below (pp. 41-42, *infra*), wrong as a general matter).

Contrary to petitioners' suggestion (GD Br. 2, Boeing Br. 36-37), the government has not sought any "forfeiture" or "penalty" against petitioners as a result of its default termination of the A-12 contract. Although the government never received a single aircraft, it has not sought the return of $1.35 billion in *liquidated* progress payments that it advanced to petitioners, nor has it sought to impose any fine or civil penalty. The contract-

ing officer's decision does allow the government to demand the return (with appropriate interest) of the *unliquidated* progress payments, *i.e.*, monies it had advanced to petitioners for work never completed. But the recovery of funds expended for uncompleted work is not plausibly characterized as a penalty. In any event, the government did not seek a recoupment order or any other form of affirmative relief *in the CFC proceedings*; it simply argued that petitioners' suit should be dismissed.

The potential availability of harsher sanctions in other cases should not affect the analysis here. Although petitioners describe the potential consequences of a default termination—including debarment from public contracting (GD Br. 7; Boeing Br. 10)—none of those collateral consequences was imposed in this case. And even if those bargained-for consequences could properly be characterized as a "forfeiture" or civil "penalty," the government would be the "moving party" in the lawsuit only if it sought to have those sanctions imposed by the court. Here, any collateral consequences that petitioners' default termination might entail are traceable to the contracting officer's decision, and they would be the same even if the CFC proceedings had never been commenced. As explained above (pp. 29-30, *supra*), suits for judicial review of agency action are no exception to the general rule that a court may not award affirmative relief on a claim that the government's proper invocation of the state-secrets privilege prevents the court from adjudicating.

C. Even If The Government Were Viewed As The "Moving Party," It Should Not Be Penalized For Properly Invoking The State-Secrets Privilege In This Civil Case

If the Court agrees (for all the reasons explained in Part B, *supra*) that the government is not the "moving party" in this civil case, *Reynolds* controls and the Due Process Clause poses no bar to entry of judgment dismissing petitioners' complaint. But even if the government is viewed as the "moving party" here, the result should be the same. The Court in *Reynolds* did not decide what disposition is appropriate when the government asserts the state-secrets privilege as the "moving party" in a civil case. For the reasons that follow, however, there is no sound rationale for automatically entering judgment against the government in that circumstance.

1. In *Reynolds*, as discussed above (p. 25, *supra*), the Court noted criminal cases from the Second Circuit holding that "the Government can invoke its evidentiary privileges only at the price of letting the defendant go free." 345 U.S. at 12 (citing *United States* v. *Andolschek*, 142 F.2d 503 (2d Cir. 1944); *United States* v. *Beekman*, 155 F.2d 580 (2d Cir. 1946)). The Court then stated that the rationale of those cases "has no application in a civil forum where the Government is not the moving party, but is a defendant only on terms to which it has consented." *Ibid.* The Court did not address the proper treatment for these purposes of civil cases in which the government *is* the "moving party."

In *Jencks* v. *United States*, 353 U.S. 657 (1957), the Court observed that "the protection of vital national interests may militate against public disclosure of documents in the Government's possession," and it pointed to

"civil causes" as examples. *Id.* at 670. The Court then contrasted those civil cases with "criminal causes," where "the Government can invoke its evidentiary privileges only at the price of letting the defendant go free." *Id.* at 670-671 (quoting *Reynolds*, 345 U.S. at 12). The Court did not suggest that the government's assertion of the state-secrets privilege similarly entails the automatic entry of an adverse judgment when the government is the "moving party" in a civil case.

In a typical federal criminal proceeding, the Executive invokes the power of the Judiciary to deprive an individual of his liberty. See *Shinseki* v. *Sanders*, 129 S. Ct. 1696, 1706 (2009). In a typical civil proceeding, by contrast, the defendant is subject to less serious potential sanctions.[12] In part because the stakes are generally so different (in kind and degree), criminal defendants are afforded greater constitutional protections than defendants in civil actions. See *In re Winship*, 397 U.S. 358, 372 (1970) ("[D]ue process * * * requires a more stringent standard for criminal trials than for ordinary civil litigation.") (Harlan, J., concurring); see also, *e.g.*, U.S. Const. Amend. VI (conferring various protections on criminal defendants). In particular, whereas withholding of exculpatory material evidence by the prosecution violates the due process rights of criminal defendants, *Brady* v. *Maryland*, 373 U.S. 83, 86-88 (1963), the defendant in a civil suit brought by the government has no comparable constitutional right. That fact alone would provide a sound basis for distinguishing criminal prosecutions from civil suits in which the government as

[12] Habeas corpus actions, in which the liberty of an individual is at stake, may present special considerations. No such considerations, however, are present in this case.

plaintiff invokes the state-secrets privilege. And whereas the "beyond a reasonable doubt" standard of proof reflects the view that significant uncertainties as to a criminal defendant's guilt should be resolved in the defendant's favor, see *Winship*, 397 U.S. at 363-364, the preponderance standard generally used in civil litigation imposes essentially equal risks of error upon the opposing parties.

For the foregoing reasons, when the government as civil plaintiff invokes the state-secrets privilege in response to a defendant's request for information, a per se rule of dismissal would be inappropriate. To be sure, if the unavailability of state-secrets information prevents the government from establishing an element of its claim seeking affirmative relief on which it bears the burden of proof, the government cannot prevail on that claim. In this case, however, the government carried its burden of proving that petitioners had defaulted on their contractual obligations. Even if the government were properly viewed as the moving party here, there would be no sound basis for extending to the civil context the rule that "the Government can invoke its evidentiary privileges only at the price of letting the defendant go free." *Reynolds*, 345 U.S. at 12.[13]

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[13] In the immigration context, the Court has sustained the use of classified information to establish an alien's inadmissibility, *Shaughnessy* v. *United States ex rel. Mezei*, 345 U.S. 206 (1953) and to deny an application for discretionary relief from deportation, *Jay* v. *Boyd*, 351 U.S. 345 (1956). See 8 U.S.C. 1225(c), 1229a(b)(4) and (c)(2); see also 8 U.S.C. 1534(e)(3)(E) (alien terrorist removal procedures). Similarly, in several other contexts, the government has submitted classified information to the courts for *ex parte* review. Even when such information has been used by courts to resolve the merits of a claim, the courts of appeals have rejected claims by private litigants that their due

2. No court in a civil case has *ever* entered judgment against the government in response to the government's proper invocation of the state-secrets privilege. Even in the three reported cases of which we are aware where the government invoked the state-secrets privilege as a civil plaintiff, none was dismissed as a result of that invocation. See *Attorney Gen.* v. *Irish People, Inc.*, 684 F.2d 928 (D.C. Cir. 1982) (civil enforcement action to compel registration under the Foreign Agents Registration Act, 22 U.S.C. 611-621 (1976)), cert. denied, 459 U.S. 1172 (1983); *United States* v. *Koreh*, 144 F.R.D. 218 (D.N.J. 1992) (seeking denaturalization of alleged Nazi collaborator); *Republic of China* v. *National Union Fire Ins. Co.*, 142 F. Supp. 551 (D. Md. 1956) (seeking insurance coverage on ships seized by Communist China).

In a variety of contexts, Congress has authorized the government to seek injunctive relief to protect national-security interests. *E.g.*, 18 U.S.C. 2339B(c) (authorizing Attorney General to "initiate civil action * * * to enjoin" provision of material support to foreign terrorist organization); 18 U.S.C. 3511(c) (authorizing Attorney General to "invoke the aid" of a district court to compel compliance with a National Security Letter). Under petitioners' theory, however, the government as civil plaintiff would be categorically foreclosed from obtaining such relief if its invocation of the state-secrets privilege prevented the district court from adjudicating an asserted defense to the government's action. This

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process rights were violated. See, *e.g.*, *National Council of Resistance of Iran* v. *Department of State*, 373 F.3d 152, 159-160 (D.C. Cir. 2004) (Roberts, J.); *Global Relief Found., Inc.* v. *O'Neill*, 315 F.3d 748, 754 (7th Cir. 2002), cert. denied, 540 U.S. 1003 (2003); see also *United States* v. *Ott*, 827 F.2d 473, 476-477 (9th Cir. 1987); *United States* v. *Belfield*, 692 F.2d 141, 148 (D.C. Cir. 1982).

Court's decisions do not support such a rule, which would subvert Congress's determination that effective civil remedies should be available.

3. Petitioners also rely on decisions of this Court stating that due process principles guarantee a civil defendant "an opportunity to present every available defense." GD Br. 30; Boeing Br. 42-43 (quoting *Lindsey* v. *Normet*, 405 U.S. 56, 66 (1972)). In addition to the fact that petitioners are not defendants here, those decision do not speak to the application of evidentiary privileges generally or the state-secrets privilege in particular.

Boeing contends (Br. 49) that "judicial treatment of other evidentiary privileges" supports its position. It is well settled, however, that a court may not impose a substantial litigation penalty, such as the dismissal of a claim, on a party that validly invokes an evidentiary privilege, even when the privileged information is "vital, highly probative, directly relevant or even go[es] to the heart of an issue." *Rhone-Poulenc Rorer Inc.* v. *Home Indem. Co.*, 32 F.3d 851, 864 (3d Cir. 1994); see 8 Charles Alan Wright et al., *Federal Practice and Procedure* § 2018 (3d ed. 2010) (collecting cases) (*Federal Practice*).

Although Boeing relies (Br. 50-51) on select lower-court discussions of the privilege against self-incrimination in civil cases, even those decisions acknowledge that dismissal of a privilege holder's case is rare and disfavored. See *Serafino* v. *Hasbro*, 82 F.3d 515, 518 n.5 (1st Cir. 1996) ("dismissal has rarely been imposed or affirmed"); *Wehling* v. *CBS*, 608 F.2d 1084, 1087 (5th Cir. 1979) ("[D]ismissing a plaintiff's action with prejudice solely because he exercises his privilege against self-incrimination is constitutionally impermissible.").

More importantly, this Court has made clear that because "the Fifth Amendment guarantees * * * the right of a person to remain silent unless he chooses to speak in the unfettered exercise of his own will, and to suffer no penalty . . . for such silence," *Spevack* v. *Klein*, 385 U.S. 511, 514 (1967) (quoting *Malloy* v. *Hogan*, 378 U.S. 1, 8 (1964)), a court may not impose "any sanction which makes assertion of the Fifth Amendment privilege 'costly,'" *id.* at 515 (quoting *Griffin* v. *California*, 380 U.S. 609, 614 (1965)). Several courts of appeals, in accord with the view of leading commentators, have held that a party's invocation of that privilege thus cannot justify dismissal of his claim. See, *e.g.*, *United States* v. *Certain Real Property and Premises Known as 4003-4005 5th Ave.*, 55 F.3d 78, 82-84 (2d Cir. 1995) ("because exercise of Fifth Amendment rights should not be made unnecessarily costly," "litigants, even if deprived of key facts through an opposing party's assertion of the Fifth Amendment, often have no recourse in the civil litigation other than to comment upon the claim of privilege in the hope of persuading the trier of fact to draw a negative inference"); *Campbell* v. *Gerrans*, 592 F.2d 1054, 1057-1058 (9th Cir. 1979) ("It is obvious that dismissal of an action is costly and therefore" "not in accord with Supreme Court decisions."); *Federal Practice* § 2018.

Boeing's reliance (Br. 51-52) on court of appeals decisions involving the attorney-client privilege is similarly misplaced. See *United States* v. *Salerno*, 505 U.S. 317, 323 (1992) ("Parties may forfeit a privilege by exposing privileged evidence, but do not forfeit one merely by taking a position that the evidence might contradict."). Unlike here, those cases involve scenarios where the privilege holder has "waived" its rights by affirmatively

relying on the privileged information to prove its claim or defense. See *Ideal Elec. Sec. Co.* v. *International Fid. Ins. Co.*, 129 F.3d 143, 151 (D.C. Cir. 1997) (holding that the privilege holder waived the attorney-client privilege by "partially disclos[ing] the allegedly privileged information in support of its claim against [the opposing party], but then assert[ing] the privilege as a basis for withholding from its opponent the remainder of the information which is necessary to defend against the claim."); *Conkling* v. *Turner*, 883 F.2d 431, 434 (5th Cir. 1989) (similar); cf. *Rhone-Poulenc*, 32 F.3d at 855-857.[14]

Whatever the proper operation of other privileges, moreover, there are strong reasons not to penalize the government for invoking the state-secrets privilege. See *Totten*, 92 U.S. at 107 (contrasting state-secrets privilege with other privileges). Even when a private litigant

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[14] The facts in *Rhone-Poulenc* are strikingly similar to those present here. In that case, two drug companies sued their insurer, alleging that the insurer had failed to honor its obligations to indemnify the companies against users' legal claims. 32 F.3d at 855. As its primary defense, the insurer alleged that the companies had failed to disclose their prior knowledge of the adverse effects of the drug. *Id.* at 856-857. To prove that defense, the insurer sought discovery of confidential communications between the pharmaceutical companies and their attorneys. *Ibid.* Although the Third Circuit did not question the relevance of the requested documents, it stated that "[r]elevance is not the standard for determining whether or not evidence should be protected from disclosure as privileged, and that remains the case even if one might conclude the facts to be disclosed are vital, highly probative, directly relevant or even go to the heart of an issue." *Id.* at 864. The critical test, the court concluded, was whether the privilege holder had "attempt[ed] to prove [a] claim or defense by disclosing or describing an attorney client communication." *Id.* at 863. Because the plaintiffs had "not interjected the advice of counsel as an essential element of a claim in [the] case," the court held that the plaintiffs could not be required to disclose the information, regardless of its value to the defense. *Id.* at 864.

is *entitled* to assert a Fifth Amendment or attorney-client privilege against disclosure of requested information, there is ordinarily no legal or prudential barrier to his voluntary waiver of that privilege. A rule under which assertion of such privileges resulted in entry of judgment against the private civil litigant, though problematic in significant respects, would at least give the litigant a choice between two legitimate options. An agency head, by contrast, cannot appropriately "waive" the state-secrets privilege by effecting disclosures that he believes will jeopardize national security. In a civil case, the Court therefore should not depart from the established understanding that, to avoid undermining the paramount collective public interest that the state-secrets privilege serves, the government should not be "punished for asserting the privilege." *Salisbury*, 690 F.2d at 975.[15]

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[15] Boeing's reliance (Br. 48-49) on proposed Federal Rule of Evidence 509 (ultimately rejected by Congress) is also unavailing. Proposed Rule 509 would have governed both civil and criminal cases, and it would have applied not just to the state-secrets privilege but also to "official information" privileges concerning, *inter alia*, intragovernmental opinions or recommendations issued in the course of policymaking, as well as certain law-enforcement investigatory files. See Proposed Fed. R. Evid. 509(a)(1)-(2), 56 F.R.D. 183, 251 (1972); see also Advisory Committee's Note to Proposed Rule 509(a)(1)-(2) and (e), *id.* at 252-254. As Boeing notes, proposed Rule 509(e) would have provided that when the government is a party to a suit and its valid assertion of a privilege deprives another party of material evidence, a court may issue any "orders which the interests of justice require, including striking the testimony of a witness, declaring a mistrial, finding against the government upon an issue as to which the evidence is relevant, or dismissing the action." *Id.* at 252. Although that menu of options would have included the authority to find in petitioners' favor on the "superior knowledge" issue, the proposed Rule would not have mandated that result. Indeed, noting an "unwillingness to allow the government's

D. Petitioners' Policy Arguments Do Not Support Entry Of Judgment Against The Government

1. Affirming the Federal Circuit's judgment will not lead to abuse of the state-secrets privilege

Petitioners suggest that, if the decision of the court of appeals is affirmed, federal officials will manipulate future litigation by invoking the state-secrets privilege in order to obtain favorable rulings on issues as to which the privilege has been claimed. GD Br. 31-33. That speculation is unfounded.

The safeguards against capricious invocation of the state-secrets privilege lie in the procedural and substantive restrictions that this Court has imposed upon the privilege, see *Reynolds*, 345 U.S. at 7-8, 10; pp. 23-24, *supra*, and in the presumption that agency heads discharge their duties conscientiously and in good faith—not in any judicially created prophylactic rule that the government must lose claims as to which the privilege has been invoked.[16] As discussed above (pp. 26-27, *supra*), the Judicial Branch should not create financial disincentives to the appropriate invocation of a privilege designed to safeguard vital national-security

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claim of privilege for secrets of state to be used as an offensive weapon against it," the Advisory Committee's Note approvingly cited *Reynolds* and *Republic of China*, 142 F. Supp. at 557, which held that the United States was *not* barred from suing ship insurers even though the government had validly invoked the state-secrets privilege with respect to information that the insurers (like petitioners here) contended could help establish a defense to the suit.

[16] Congress has considered various proposals to regulate the government's assertion of the state-secrets privilege—*e.g.*, State Secrets Protection Act, S. 2533, 110th Cong. 2d Sess. (2008); State Secrets Protection Act, S. 417, 111th Cong. 1st Sess. (2009)—but has not passed any such legislation.

information. And petitioners point to no pattern of abuse despite the thousands of contracts awarded by the Defense Department and military services each year. Notably, petitioners do not contend that the government improperly invoked the privilege in this case. Boeing Br. 27; GD. Br. 35-36.[17]

On September 23, 2009, the Attorney General issued Policies and Procedures Governing Invocation of the State Secrets Privilege, http://www.justice.gov/opa/documents/state-secrets-privilege/pdf (State Secrets Policy), which provides additional safeguards. Under that policy, the Department of Justice will defend an assertion of the state-secrets privilege and seek dismissal of a claim only when "necessary to protect against the risk of significant harm to national security." *State Secrets Policy* 1. "The Department will not defend an invocation of the privilege in order to: (i) conceal violations of the law, inefficiency, or administrative error; (ii) prevent embarrassment to a person, organiza-

[17] Although petitioners acknowledge that they have no basis for challenging the government's invocation of the state-secrets privilege in this case, they nevertheless accuse the government of vaguely defined abuses relating to its treatment of classified information during the course of the litigation. See GD Br. 13-14, 25-26, 46, 53-54; Boeing Br. 16 n.6, 37. Those accusations are unfounded. The Federal Circuit reviewed the same allegations and rejected the CFC's statement that the government had used the privileged information "for tactical purposes involving the merits of plaintiffs' superior knowledge claim." J.A. 568 n.5. The Federal Circuit explained that the government attorneys' alleged review of privileged information was "entirely irrelevant to whether there would be a 'reasonable danger' to national security if the information is released to someone new." J.A. 568. Three years later, the CFC found that "[d]espite *everyone's best efforts*, the risk of compromising national secrets is too serious to proceed to trial." Pet. App. 381a (emphasis added).

tion, or agency of the United States government; (iii) restrain competition; or (iv) prevent or delay the release of information the release of which would not reasonably be expected to cause significant harm to national security." *Id.* at 2. In addition, the Department will defend an assertion of the privilege in court only with the personal approval of the Attorney General following review and recommendations from senior Department officials. *Id.* at 3. See *Mohamed* v. *Jeppesen Dataplan, Inc.*, 614 F.3d 1070, 1080, 1090 (9th Cir. 2010) (en banc).[18]

The rule that petitioners advocate, by contrast, would itself be susceptible to manipulation by private parties. As discussed above (p. 27, *supra*), a contractor that challenges the government's termination of a contract for default could raise a superior-knowledge claim simply to induce the government to invoke the state-secrets privilege. Cf. *Tenet*, 544 U.S. at 11. In those circumstances, automatic invalidation of a default termination—or, more generally, a requirement that courts rule against the government on any issue to which state-

[18] Because the September 2009 policy applies only to cases in which the government invokes the state-secrets privilege after October 1, 2009, *State Secrets Policy* 1, it does not govern the Department's litigation of this case. In any event, the courts below determined that the government had properly invoked the state-secrets privilege here, and petitioners did not challenge that determination in their petitions for writs of certiorari. The questions on which this Court granted certiorari do not encompass the question whether the privilege was properly invoked. Because petitioners nevertheless seek to cast doubt on the propriety of the government's assertion of the privilege in this case (*e.g.*, Boeing Br. 37), we encourage the Court to examine the classified declarations filed by the government and reviewed by the CFC and Federal Circuit in this case. Those classified declarations, which appear in unclassified form at J.A. 516-523 and 974-981, will be made available at the Court's request.

secrets material would potentially be relevant, including issues on which a private plaintiff bears the burden of proof—would inappropriately "punish[] [the government] for asserting the privilege." *Salisbury*, 690 F.2d at 975.

2. Affirming the Federal Circuit's judgment will not undermine defense contracting

There is likewise no sound basis for the speculation of petitioners and their amici that defense contracting will be undermined if the judgment of the court of appeals is affirmed. GD Br. 48-49; Chamber of Commerce Amicus Br. 6-9; NDIA Amicus Br. 11-17. The government has a strong interest in attracting contractors to ensure that our Nation's security and other needs are met, and it disagrees entirely with such speculation. Moreover, contractors like petitioners are highly sophisticated entities that can protect themselves against undue risk in their negotiation of future contracts.

In this case, for example, petitioners were allowed (even under the court of appeals' decision) to retain $1.35 billion in progress payments, notwithstanding their failure to deliver a single aircraft, because they successfully negotiated contract terms that permitted "liquidation" of certain progress payments prior to completion of all contract work. J.A. 115-116; see p. 5, *supra*. The FSED contract also contained a clause specifying what information the government was required to share with petitioners. J.A. 136-140. Petitioners could have sought to include in that clause the classified information that they now allege was necessary to perform the contract, and they could have declined to enter into the contract if the government had refused to promise them access to such information.

Petitioners cite no evidence that contractors have refused to deal with the government as a result of the decision of the court of appeals on the "unique facts of this case." Pet. App. 33a. To the contrary, petitioners themselves, as well as other contractors, have entered into long-term development and production contracts for military aircraft and other equipment for billions of dollars since the government's 1993 invocation of the state-secrets privilege in this suit. See, *e.g.*, *Boeing Receives Multi-Year Contract from U.S. Navy for 124 F/A-18 and EA-18 Aircraft* (Sept. 28, 2010), http://boeing.mediaroom.com/index.php?s=43&item=1442. The absence of any apparent adverse impact on contractors' willingness to deal with the government is unsurprising, as it has been clear at least since *Reynolds* that the government as civil defendant may invoke the state-secrets privilege without suffering the automatic entry of an adverse judgment. And petitioners cite no civil case involving the government as either defendant or plaintiff in which the assertion of the state-secrets privilege was held to entail that consequence.

Finally, nothing prohibits contractors like petitioners from requesting a clause in future contracts that would assign the risk of a state-secrets invocation to the government—*e.g.*, by providing that if the contractor is terminated for default, and a subsequent invocation of the state-secrets privilege precludes access to information which could have supported a valid excuse for nonperformance, the default will be treated as one for convenience. Or contractors could request specific procedures to facilitate the consideration of sensitive information in the event of a dispute; for example, the Navy in limited circumstances has agreed to alternative dispute resolu-

tion procedures for contracts involving special-access programs.

For all these reasons, there is no reason to suppose that a decision affirming the judgment below would change government contractors' perceptions of the risks to which they are subject when they perform work on projects implicating national-security concerns.

E. If This Court Reverses The Judgment Of The Court Of Appeals, It Should Remand For Consideration Of The Government's Other Preserved Defenses To The Superior-Knowledge Claim

1. Before it invoked the state-secrets privilege, the government had sought dismissal of petitioners' claim that their default could be excused based on the government's alleged failure to disclose to them information contained in "classified, compartmented weapon system development programs." J.A. 451-452. The government relied in part on the general legal proposition that there can be no implied duty to share highly classified information. The CFC ruled that the government at least had a duty to provide petitioners a "general warning" about potential problems, if not the classified information itself. Pet. App. 354a n.7. In response, the government contended, *inter alia*, that the warnings it raised at the time petitioners submitted their proposal to win the A-12 contract satisfied any such duty and that no further "general warning" would have aided petitioners. J.A. 896-900, 909-913, 1275-1280.

The government further argued that recognition of an implied duty to share classified information would conflict with the express terms of the A-12 contract. J.A. 895-896, 1275-1276. As noted above (p. 6, *supra*), the contract specifically identified the information that

the government agreed to provide petitioners. J.A. 136-140. It is well established that an implied duty "cannot expand a party's contractual duties beyond those in the express contract or create duties inconsistent with the contract's provisions." *Precision Pine & Timber, Inc.* v. *United States*, 596 F.3d 817, 831 (Fed. Cir. 2010), petition for cert. pending, No. 10-341 (filed Sept. 8, 2010).

The government preserved those threshold legal arguments by raising them in the first two appeals to the Federal Circuit. See J.A. 893-916, 1274-1292. (The last appeal did not involve the superior-knowledge claim.) The Federal Circuit never passed on those arguments because it resolved the superior-knowledge issue on the basis of the state-secrets privilege. If this Court were to reverse the Federal Circuit's judgment, however, those defenses would become ripe for appellate review. The court of appeals should be allowed to consider those issues before the government is subjected to an adverse judgment.[19]

2. Because those defenses remain pending, GD's request that this Court reinstate the 1998 CFC damages award—$1.2 billion, plus interest, after offsetting $2.7 billion in liquidated and unliquidated payments already

[19] GD notes (Br. 55) that the "government's opposition to certiorari did not question the trial court's rulings that the government had a duty to share its knowledge with the Contractors." But that issue was not encompassed by the questions presented in the petition, which challenged only the consequences of the Federal Circuit's holding that the superior-knowledge claim was nonjusticiable. In any event, the government does not ask this Court to rule on its legal defenses to petitioners' superior-knowledge claim, but simply to leave them open on remand if the Court reverses or vacates the judgment below.

made to petitioners (J.A. 884-885)—is premature.[20] Moreover, the Federal Circuit never ruled on the government's challenge to that award on the merits, as it had vacated the award as moot in 1999 in light of its reversal of the CFC's underlying determination of government liability and conversion to a termination for convenience. Pet. App. 271a, 278a-279a. The CFC has had no occasion to reconsider its prior ruling, which it also regarded as moot after further proceedings on remand. *Id.* at 174a. The government therefore should be permitted at least to obtain appellate review on the merits of that multi-billion dollar award before being subjected to it.[21]

---

[20] Notably, Boeing does not join GD in making such an untenable request.

[21] On the merits, the CFC's 1998 damages judgment is seriously flawed. The contract's termination-for-convenience provision allows for recovery of the costs of performance, plus profit, without regard to whether work was completed or whether work was acceptable, *except* if the contractor was already performing at a loss. 48 C.F.R. 52.249-2(f)(2)(iii). "If it appears that the contractor would have suffered a loss on the entire contract * * * the contractor would not obtain a profit, and its cost recovery is reduced according to the rate of loss." Pet. App. 282a. The plain language of the contract therefore *requires* adjustment for the loss rate to ensure that a convenience termination does not place petitioners in a better position than they would have occupied if they had performed the contract. See *Rumsfeld* v. *Applied Cos.*, 325 F.3d 1328, 1336 (Fed. Cir.) (citing *Miller* v. *Robertson*, 266 U.S. 243, 260 (1924)), cert. denied, 540 U.S. 981 (2003). Here, it is undisputed that petitioners were performing at a significant loss at the time of termination and that, by their own admission, they could not have absorbed the contract's projected losses. See pp. 7-9, *supra*. In addition, petitioners bear the burden of establishing the amount of any convenience-termination recovery. *Lisbon*, 828 F.2d at 767. Because the CFC found that the nonjusticiable superior-knowledge claim was related to petitioners' convenience-termination claim for damages, the CFC should have dismissed that damages claim. J.A. 901-903, 917-921, 1058-1059.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

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DECEMBER 2010

APPENDIX

1. 28 U.S.C. 1491 provides in pertinent part:

Claims against United States generally; actions involving Tennessee Valley Authority

(a)(1) The United States Court of Federal Claims shall have jurisdiction to render judgment upon any claim against the United States founded either upon the Constitution, or any Act of Congress or any regulation of an executive department, or upon any express or implied contract with the United States, or for liquidated or unliquidated damages in cases not sounding in tort. For the purpose of this paragraph, an express or implied contract with the Army and Air Force Exchange Service, Navy Exchanges, Marine Corps Exchanges, Coast Guard Exchanges, or Exchange Councils of the National Aeronautics and Space Administration shall be considered an express or implied contract with the United States.

(2) To provide an entire remedy and to complete the relief afforded by the judgment, the court may, as an incident of and collateral to any such judgment, issue orders directing restoration to office or position, placement in appropriate duty or retirement status, and correction of applicable records, and such orders may be issued to any appropriate official of the United States. In any case within its jurisdiction, the court shall have the power to remand appropriate matters to any administrative or executive body or official with such direction as it may deem proper and just. The Court of Federal Claims shall have jurisdiction to render judgment upon any claim by or against, or dispute with, a contractor

arising under section 10(a)(1) of the Contract Disputes Act of 1978, including a dispute concerning termination of a contract, rights in tangible or intangible property, compliance with cost accounting standards, and other nonmonetary disputes on which a decision of the contracting officer has been issued under section 6 of that Act.

* * * * *

2. 41 U.S.C. 605 provides in pertinent part:

Decision by contracting officer

(a) Contractor claims

All claims by a contractor against the government relating to a contract shall be in writing and shall be submitted to the contracting officer for a decision. All claims by the government against a contractor relating to a contract shall be the subject of a decision by the contracting officer. Each claim by a contractor against the government relating to a contract and each claim by the government against a contractor relating to a contract shall be submitted within 6 years after the accrual of the claim. The preceding sentence does not apply to a claim by the government against a contractor that is based on a claim by the contractor involving fraud. The contracting officer shall issue his decisions in writing, and shall mail or otherwise furnish a copy of the decision to the contractor. The decision shall state the reasons for the decision reached, and shall inform the contractor of his rights as provided in this chapter. Specific findings of fact are not required, but, if made, shall not be binding in any subsequent proceeding. The authority of

this subsection shall not extend to a claim or dispute for penalties or forfeitures prescribed by statute or regulation which another Federal agency is specifically authorized to administer, settle, or determine. This section shall not authorize any agency head to settle, compromise, pay, or otherwise adjust any claim involving fraud.

(b) Review; performance of contract pending appeal

The contracting officer's decision on the claim shall be final and conclusive and not subject to review by any forum, tribunal, or Government agency, unless an appeal or suit is timely commenced as authorized by this chapter. Nothing in this chapter shall prohibit executive agencies from including a clause in government contracts requiring that pending final decision of an appeal, action, or final settlement, a contractor shall proceed diligently with performance of the contract in accordance with the contracting officer's decision.

* * * * *

3. 41 U.S.C. 609 provides in pertinent part:

Judicial review of board decisions

(a) Actions in United States Court of Federal Claims; district court actions; time for filing

(1) Except as provided in paragraph (2), and in lieu of appealing the decision of the contracting officer under section 605 of this title to an agency board, a contractor may bring an action directly on the claim in the United States Court of Federal Claims, notwithstanding any contract provision, regulation, or rule of law to the contrary.

(2) In the case of an action against the Tennessee Valley Authority, the contractor may only bring an action directly on the claim in a United States district court pursuant to section 1337 of title 28, notwithstanding any contract provision, regulation, or rule of law to the contrary.

(3) Any action under paragraph (1) or (2) shall be filed within twelve months from the date of the receipt by the contractor of the decision of the contracting officer concerning the claim, and shall proceed de novo in accordance with the rules of the appropriate court.

* * * * *

REPLY BRIEF

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In The Supreme Court of the United States

♦

GENERAL DYNAMICS CORPORATION,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

♦

THE BOEING COMPANY,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

♦

On Writ Of Certiorari To The United States Court Of Appeals For The Federal Circuit

♦

REPLY BRIEF OF PETITIONER THE BOEING COMPANY

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CORPORATE DISCLOSURE STATEMENT

Petitioner's Rule 29.6 disclosures appear in its opening brief (at ii). There are no changes to those disclosures.

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ARGUMENT

The defining characteristic of both alternative rules the Government asks the Court to adopt is that the Government will *never* be barred from litigating a claim or defense as a result of its own decision to invoke the state secrets privilege, and its opponent will *always* suffer the adverse litigation consequences of protecting the Nation's secrets. The Government's primary submission – that "moving party" status, as this Court used the term in *United States v. Reynolds*, 345 U.S. 1, 12 (1953), simply turns on which party filed suit in the Court of Federal Claims ("CFC") – ignores the fact that the governing statute *requires* the contractor to initiate proceedings in the CFC (or before a board of contracting appeals ("BCA")) in *all* Government contract disputes, regardless of which side is asserting the claim and seeking affirmative relief. Under this statutory scheme, a contractor's only avenue for presenting a defense to a Government claim is to put the Government to its burden of proving that claim in proceedings initiated by the contractor before the CFC or a BCA. Thus, the rule the Government advances necessarily means that, regardless of who is bringing the claim for affirmative relief and who is defending, the contractor's claim or defense will *always* be barred by the state secrets privilege and the Government's claim or defense *never* will.

The same is true of the alternative rule proposed by the Government. Specifically, the Solicitor General urges the Court to hold that in cases, like this one,

where the Government is the moving party advancing a civil claim and the opposing party's ability to defend is substantially prejudiced by invocation of the state secrets privilege, the Government's claim should be permitted to proceed. Yet the Government does not deny that when the shoe is on the other foot, it invariably argues that a private party's civil claim *against* it must be dismissed whenever *the Government's* defense is substantially prejudiced by the need to protect state secrets.

In contrast to the "Government always wins" submissions of the Solicitor General, the rule urged by the Contractors applies evenhandedly to both sides, does not penalize the Government for the Executive's decision to invoke the state secrets privilege, and vindicates the fundamental due process principle that a claim for affirmative relief may not proceed if the opposing party's ability to defend is substantially prejudiced.

I. The Government Is the Moving Party.

Despite the fact that the Government seeks to sustain the Contracting Officer's decision for the Government on its default-termination claim and to recover $1.35 billion plus interest from the Contractors based on that decision, the Government argues that it is not the moving party on that claim. In support of this argument, the Government repeatedly invokes the Contractors' separate request to recover their unreimbursed costs in the proceedings below

and asserts that the Government, by contrast, sought no "affirmative relief" *from the CFC*. In so arguing, the Government asks this Court to close its eyes to the procedural posture of this case and the statutory framework in which it arises, and to ignore the reality that the Government is the party seeking affirmative relief on the underlying default-termination claim at issue here.

A. The Contractors' Assertion of a Separate Claim for Costs Does Not Make Them the Moving Parties on the Government's Default-Termination Claim.

The Government repeatedly emphasizes the Contractors' request to recover their unreimbursed costs in the proceedings below (even though that claim is not before this Court) in an effort to obscure the fact that it is the Government, and only the Government, that seeks affirmative relief on the default-termination claim (which is before the Court). Under well-settled precedent, however, these are separate claims that belong to (and must be asserted and proved by) different parties, and must be (and were) separately submitted to and decided by the Contracting Officer and the courts. The Contractors do not dispute that they may be the moving party on their claim for costs, or that the same principles they urge this Court to apply to the Government's default-termination claim might also apply to the Contractors' claim for costs. It is abundantly clear, however, that the Government, not the Contractors, is the

moving party on its own default-termination claim. And the issue before this Court is not, as the Government would have it, whether the assertion of the state secrets privilege may properly bar the Contractors from pursuing their claim for costs against the Government, but rather whether the assertion of the privilege may bar the Contractors from presenting their superior-knowledge *defense* to the Government's default-termination claim.

1. In the proceedings below, the Contractors did seek their unreimbursed costs of performance from the Government. Contrary to the Government's intimations, however, they sought this affirmative relief not in connection with the Government's default-termination claim, but rather as a separate claim to be litigated and decided by the court only in the event that the Government's claim was rejected and the default termination was converted into a termination for convenience.

As the CFC correctly recognized, it is well settled that "[t]ermination for default is a government claim, and termination for convenience is a separate contractor claim," and that "a termination for convenience cost recovery claim . . . is distinct from the Government's claim for return of unliquidated progress payments, which accompanies the default termination." *McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 285, 289, 291 (1997); *see also Malone v. United States*, 849 F.2d 1441, 1443-44 (Fed. Cir. 1988) (so holding). The Government cannot, and

does not, deny that default termination is a Government claim that must be asserted by the Government, decided by the Contracting Officer, and justified by the Government if the contractor puts the Government to its proof before a BCA or the CFC. *See* Boeing Br. 7-9. A claim for costs, by contrast, is a separate claim that belongs to – and must be asserted and proved by – the contractor. Thus, if a contractor wishes not only to defend against the Government's default-termination claim but also to seek its unreimbursed costs, the contractor must expressly file its own separate claim for those costs with the Contracting Officer and, if that claim is denied, prove its costs before a BCA or the CFC. A contractor is not required, however, to file a claim for costs to defend against a default-termination claim, but if it does not do so, it will not be entitled to any affirmative relief even if it successfully defends against the Government's default-termination claim. *See Malone*, 849 F.2d at 1443-44 ("Because the default termination in this case was a government claim, Malone properly appealed it without first submitting its own claim to the CO."); *Boeing Co. v. United States*, 31 Fed. Cl. 289, 292-93 (1994) ("contractor claims seeking termination for convenience costs and equitable adjustments are not pending before the court merely because a complaint has previously been filed seeking reversal of a termination for default and demand for return of progress payments").

Thus, in this case, the Contractors submitted their request for costs to the Contracting Officer and

then to the CFC as a claim for relief distinct from their defense to the Government's default-termination claim, and that claim was separately decided by both the Contracting Officer and the CFC. *See McDonnell Douglas*, 37 Fed. Cl. at 287-88, 290-91 (detailing the different claims submitted to and decided by the Contracting Officer); Pet. App., No. 09-1298 ("Pet. App.") 382a-429a (1996 CFC decision overturning default termination); Pet. App. 280a-342a (1998 CFC decision on Contractors' claim for costs after separate, subsequent litigation of this claim). Indeed, because the Contracting Officer had not yet rejected the Contractors' claim for costs when they initially filed suit, the CFC's jurisdiction was initially limited to consideration of the Government's default-termination claim. "Not until the cost recovery claim was deemed denied [by the Contracting Officer] and included in plaintiffs' amended complaint . . . did [the CFC] have jurisdiction to review that claim." *McDonnell Douglas*, 37 Fed. Cl. at 291.

2. As the Government appears to recognize, *see* U.S. Br. 28, the party seeking affirmative relief is the moving party within the meaning of *Reynolds*. And there can be no question that the Government, not the Contractors, seeks such relief on the default-termination claim in this case. Indeed, the Government sought and obtained "a final decision by the contracting officer demanding return of unliquidated progress payments" from the Contractors in the amount of $1.35 billion plus interest in connection with its default-termination claim, *McDonnell*

Douglas, 37 Fed. Cl. at 287, and it has repeatedly indicated its intention to enforce this demand if its default-termination claim is upheld by the courts, *e.g.*, JA 339-41. While the Government claims that the affirmative relief it seeks is merely "a happenstance of the timing of payments under the A-12 contract," U.S. Br. 19, there can be no doubt that any party that seeks to alter the status quo by legally compelling another to pay it money is a "moving party" within the meaning of *Reynolds*. And a court should not sanction such affirmative relief when the Government's invocation of the state secrets privilege renders the court unable to determine with confidence that it is warranted. *See* Boeing Br. 47-48.

More generally, as the courts have long recognized and the Government concedes, U.S. Br. 31, default termination is a Government claim, whether before the Contracting Officer, the CFC, or a BCA. *See Malone*, 849 F.2d at 1443-44; *Lisbon Contractors, Inc. v. United States*, 828 F.2d 759, 763-65 (Fed. Cir. 1987). The gravamen of such a claim is the Government's contention that a contractor has committed a serious contractual breach, *see Malone*, 849 F.2d at 1443, and when the Government proves such a claim, it is entitled to affirmatively seek monetary relief amounting to a forfeiture from the contractor, as well as a number of other severe penalties, up to and including debarment from public contracting. *See* Boeing Br. 9-11. Finally, whether before a BCA or the CFC, the Government bears the burden of proving

that default termination was justified. *See Lisbon*, 828 F.2d at 763-65. All of these well-established legal principles further confirm that the Government is the moving party on its default-termination claim.

3. The Government labors mightily to recharacterize the Contractors' superior-knowledge defense as an affirmative contractor claim bearing only the most tangential relationship to the Government's default-termination claim. *See, e.g.*, U.S. Br. 33-34. But the Contractors plainly raised this contention as a defense to the Government's default-termination claim. Under the Federal Acquisition Regulation ("FAR"), the Government's breach of its superior-knowledge duty may – and in this case does – excuse a contractor's alleged default. 48 C.F.R. § 52.249-9(g) (1984) [JA 226]; *see Hardeman-Monier-Hutcherson v. United States*, 458 F.2d 1364, 1369-73 (Ct. Cl. 1972). Accordingly, the Government, the CFC, and the court of appeals all recognized the Contractors' superior-knowledge argument as a *defense* in the proceedings below. *See, e.g.*, Pet. App. 182a (listing superior knowledge among "the Contractors' defenses"); Pet. App. 243a (same); JA 923 (Government's pretrial submission listing "the Navy's alleged withholding of superior knowledge" among the "anticipated affirmative defenses"); JA 1274 (Government's brief to court of appeals defending trial court's handling of "the Defense of Superior Knowledge"). Indeed, even the Government's strained attempts in this Court to characterize the Contractors' superior-knowledge contentions as an affirmative claim for relief only confirm

that they are in fact a defense to its default-termination claim. *See, e.g.*, U.S. Br. at (I) (describing these contentions as "one of petitioners' claims seeking to excuse their default").[1]

It does not matter that the Contractors bear the burden of proving their superior-knowledge contentions because, as relevant here, the Contractors assert them not to obtain affirmative relief but rather to defend against the Government's default-termination claim. Indeed, it is not at all uncommon for a party to bear the burden of proof on a defense to a moving party's claim. For example, criminal defendants bear the burden of proof on a variety of affirmative defenses, yet the Government remains the moving party because it is seeking to impose an affirmative punitive sanction, which the defendant seeks only to avoid. And under *Reynolds* and *Jencks v. United States*, 353 U.S. 657 (1957), the Government surely could not maintain a criminal prosecution while invoking the state secrets privilege to bar litigation of a prima facie valid affirmative defense. To the contrary, as the Government recognizes, the

[1] To be sure, the Contractors also sought an equitable adjustment based on the Government's failure to share its superior knowledge in connection with their separate claim to recover reasonable profits on work completed in the event the default termination was converted to one for convenience But the fact that they made this additional argument does not change the fact that they also raised superior knowledge as an essential defense to the Government's default-termination claim. *See* Boeing Br. 13-15.

party seeking affirmative relief remains the moving party, "even if the [opposing party] bears the burden of proof on some subsidiary questions." U.S. Br. 33.

B. The Government's Assertion That It Sought No Affirmative Relief *from the CFC* Is Irrelevant.

The Government also repeatedly claims that it sought no affirmative relief from the Contractors in the *Court of Federal Claims*. In so arguing, it asks this Court to ignore the facts that it seeks to recover billions of dollars from the Contractors as affirmative relief on its default-termination claim, that it has already issued a unilateral decision awarding itself this relief, and that, pursuant to the unique, Government-designed statutory framework that controls this case, that decision had the force of law and would have been "final and conclusive" had the Contractors not put the Government to its proof on its default-termination claim by timely bringing this suit in the CFC. 41 U.S.C. § 605(b); *see also* § 609(a)(1).

The Government does not – indeed cannot – seriously dispute that it was the moving party or that it sought and obtained affirmative relief on a Government claim *before the Contracting Officer*. Indeed, the Contracting Officer determined that default termination was appropriate and ordered the Contractors to pay the Government $1.35 billion plus interest.

1. Although the Government is thus plainly the moving party on the underlying default-termination claim at issue here, it nevertheless argues that it was not the moving party *in the CFC*. In support of this contention, it repeatedly argues that if it prevails in this lawsuit the result will simply be the same as if no lawsuit had ever been filed and that "any collateral consequences that petitioners' default termination might entail are traceable to the contracting officer's decision." U.S. Br. 37-38. But given the force of law afforded Contracting Officer decisions by the Contract Disputes Act ("CDA"), this argument plainly rings hollow: had this suit never been filed, the Government could have obtained all of the affirmative relief it seeks – $1.35 billion plus interest from the Contractors – simply on the strength of the Contracting Officer's decision, which would have been conclusive in a suit by the Government to enforce the decision and obtain payment from the Contractors directly, or in an action by the Contractors challenging the Government's offset of the payment against money due them under other contracts. *See Seaboard Lumber Co. v. United States*, 903 F.2d 1560, 1562 & n.4 (Fed. Cir. 1990) (unless contractor puts Government to its proof before BCA or CFC, Contracting Officer's decision becomes final and "[t]he government may obtain a judgment on the basis of such decision in a state or federal court without litigating the merits"); *United States v. Suntip Co.*, 82 F.3d 1468, 1474 (9th Cir. 1996) (finding suits to enforce Contracting Officers' decisions "similar to a suit on a judgment, because the merits of the officers' decisions

are not subject to attack"); *United States v. Kasler Elec. Co.*, 123 F.3d 341, 345-46 (6th Cir. 1997) (similar).

2. The Government similarly asserts that it was not the moving party in the CFC because it did nothing more than "simply urge[] dismissal" of the Contractors' suit. U.S. Br. 35. But this action (or substantively identical proceedings before a BCA) provides the Contractors' only access to a neutral tribunal to defend against the affirmative relief the Government sought to award itself. Further, the Government contends that dismissal of the Contractors' action would, without more, entitle it to enforce the Contracting Officer's decision. Accordingly, it would have been unremarkable had the Government merely urged dismissal of the action filed in the CFC, for according to the Government, there was no need for it to do anything else to preserve its ability to collect the award of $1.35 billion plus interest ordered by its Contracting Officer.[2]

In short, the fact that the Contractors put the Government to its proof on its default-termination claim by bringing this action in the CFC, as required by the CDA, no more changes the Government's status as the moving party on this claim than it changes the fact that default termination is a

[2] As Petitioner General Dynamics explains, moreover, *see* General Dynamics Reply 2, 10, the Government did not simply urge dismissal of the Contractors' challenge to the default termination. Rather, it urged the CFC to sustain the default termination.

Government claim on which it bears the burden of proof. Indeed, in light of the unique framework Congress has created for adjudicating Government claims against private contractors, moving-party status simply cannot turn on who brings the CDA action in court. As the Government concedes, *see* U.S. Br. 31, under the CDA and the Tucker Act, the Government cannot initiate proceedings in court for any contract dispute; rather, it must present its claims to the Contracting Officer. Far from disadvantaging the Government, this unique procedural rule was designed by the Government and operates to its clear benefit: the Contracting Officer, who is a Government employee subject (as this case well illustrates, *see* Boeing Br. 5-6) to Government supervision and control, can render a legally enforceable award against the contractor. Accordingly, if moving-party status depends not on who is seeking affirmative relief on the underlying claim, but solely on who initiated the action in the CFC, the Government has structured the game board to ensure that it can *never* be the moving party in contract disputes, and that private contractors will *always* bear the full consequences of the Government's invocation of the state secrets privilege in such disputes.

The Government offers no good reason in support of its "heads we win, tails you lose" approach to moving-party status and the allocation of the consequences of the invocation of the state secrets privilege. In contrast, basic principles of due process and fundamental fairness strongly support the rule

embraced by precedent and urged by the Contractors – that a claim for affirmative relief (whether brought by – or against – the Government or anyone else) may not proceed if invocation of the state secrets privilege substantially prejudices the opposing party's ability to defend.

3. In light of the unique statutory framework governing this case, the Government is plainly not similarly situated to a private party to a contract who withholds performance because it believes its counterparty has failed to perform, as the Government asserts, *see* U.S. Br. 36. Unlike the Government, such a party cannot unilaterally issue a judgment against its counterparty that will have the force of law unless promptly challenged in court.

4. Similarly, although the Government cites various cases for the proposition that "[p]ersons who challenge adverse agency action" are treated as moving parties, *see* U.S. Br. 29, none of those cases addressed a challenge to an administrative decision *having the force of law*, let alone a decision *granting the Government affirmative relief on a Government claim*. And certainly none of those cases addressed a circumstance where the Government bears the burden of proving to the courts, *de novo*, its entitlement to such relief. Indeed, to the extent those cases bear on the issues presented here, they support the rule sought by the Contractors. *See, e.g.*, *Sterling v. Tenet*, 416 F.3d 338, 347-48 (2005) (dismissing claim because, *inter alia*, Government could not "defend against it, without presenting evidence on

topics that are state secrets"); *Kasza v. Browner*, 133 F.3d 1159, 1166 (1998) ("if the privilege deprives the *defendant* of information that would otherwise give the defendant a valid defense to the claim, then the court may grant summary judgment to the defendant") (quotation marks omitted); *Edmonds v. United States Dep't of Justice*, 323 F. Supp. 2d 65, 81-82 (D.D.C. 2004) (dismissing claims because, *inter alia*, defendants could not defend without disclosing privileged information).

II. There Is No Basis for the Government's Alternative Rule that the Government – and Only the Government – May Proceed with a Civil Claim when Its Invocation of the State Secrets Privilege Substantially Prejudices the Opposing Party's Ability to Defend.

The Government maintains that even if it is the moving party on its default-termination claim, the foreclosure of the Contractors' superior-knowledge defense as a result of the Government's assertion of its state secrets privilege does not warrant dismissal of its default-termination claim. The Government's argument rests largely on a hyperbolic mischaracterization of the Contractors' position. The Contractors do not contend that the Government's claim should *automatically* be dismissed to penalize the Executive's assertion of the privilege. Rather, they contend that dismissal of an affirmative claim for relief, whether brought by the Government or a private

party, will be necessary only as a last resort when there is no adequate alternative that would protect the state secret without substantially prejudicing the opposing party's ability to defend. Not only is this rule compelled by basic principles of due process and fairness, it is also the same rule repeatedly and successfully invoked by the Government when it furthers the Government's own interest, and there is no principled basis for the Government's proposed, self-serving exemption from that rule when it does not.

A. The Government Mischaracterizes the Rule Sought by the Contractors.

The Government's arguments rest on a pervasive distortion of the Contractors' position. The Contractors do not contend, as the Government would have it, that a court should "automatically enter[] judgment against the government" whenever it "asserts the state-secrets privilege as the 'moving party' in a civil case." U.S. Br. 39; *see also* U.S. Br. 20, 26, 39-41, 49, 51. Rather, they contend that dismissal is warranted if, but only if, the opposing party's ability to defend against an affirmative claim for relief is substantially prejudiced by the Government's assertion of privilege, and there is no adequate alternative remedy to ensure the integrity of the adjudicative process. Significantly, the Contractors' proposed rule would apply neutrally, without regard to whether the

Government is bringing a claim for affirmative relief or defending against a claim brought by a private party.

1. The Contractors were substantially prejudiced when the Government's assertion of privilege foreclosed their superior-knowledge defense to the Government's default-termination claim, potentially entitling the Government to billions of dollars. The Government frets about "marginal or meritless" defenses, U.S. Br. 18, 20, 26, but the trial court determined that the Contractors had "made an impressive showing that they can present a prima facie case" for their defense using only the non-privileged evidence available to them. JA 623; *see also* Boeing Br. 16-19, 22-23. That conclusion was not vitiated by the trial court's later conclusion that it "cannot know whether [the superior-knowledge defense] has merit." Pet. App. 246a; *cf.* U.S. Br. 16 n.8. The court's point was merely that, without the privileged evidence, it could not resolve the *ultimate* merits of the defense. *See* Pet. App. 245a.

Relying on a selective, one-sided recitation of the facts, the Government nonetheless tries to cast doubt on the trial court's undisturbed conclusion that the Contractors' superior-knowledge defense was legally sound and well supported by the available, non-privileged evidence. *See* U.S. Br. 3-7, 52-53; *cf., e.g.*, Pet. App. 354a n.7; JA 389-94. But the Government does not – and cannot – contend that the Contractors' superior-knowledge defense is pretextual. And in all events, as the Government eventually admits, the

merits of the Contractors' superior-knowledge defense are not before this Court and, to the extent the Government has preserved them, its challenges to the sufficiency of the defense may be considered on remand. *See* U.S. Br. 53 & n.19.

2. The Contractors initially did not seek dismissal of the Government's default-termination claim. Rather, the Contractors urged the trial court to allow their defense to proceed without the privileged evidence. Pet. App. 245a; *see also* Pet. App. 355a, 367a; JA 769. The *Government* resisted further litigation concerning superior knowledge because of the risk of inadvertent disclosure of privileged evidence. Pet. App. 205a-06a; Pet. App. 344a n.1, 355a, 374a-76a; JA 1233-35. And before barring the superior-knowledge defense, the trial court doggedly "searched for ways" to litigate it "on the basis of [the Contractors'] *prima facie* evidence" without risking the disclosure of state secrets. Pet. App. 369a; *see, e.g.*, Pet. App. 244a; Pet. App. 355a-59a; JA 768-69. The trial court ultimately determined that the risk of disclosure was unacceptable, and so it precluded the Contractors from asserting their prima facie valid defense. It has thus become clear that there is no adequate alternative remedy to dismissal of the Government's default-termination claim that will ensure the integrity of the adjudicative process.

B. The Contractors Do Not Seek to "Penalize" the Government for Asserting the Privilege.

The Government's repeated claim that the Contractors impermissibly seek to "penalize" it for asserting its state secrets privilege, *see* U.S. Br. 18, 22, 27, 39, 43-46, 50, depends largely upon the Government's mischaracterization of the Contractors' proposed rule. Because the Government's default-termination claim would be dismissed not automatically, but only in light of the substantial prejudice to the Contractors' ability to defend and the lack of any adequate alternative, dismissal here is not a "penalty," but rather a necessary, proper, and neutral remedy to ensure due process and the integrity of the adjudicative proceedings, as a variety of authorities have recognized.

1. The three lower court decisions cited by the Government in which "the government invoked the state-secrets privilege as a civil plaintiff," U.S. Br. 42, actually support the Contractors' position that dismissal of a civil Government claim is warranted under the present circumstances. In *Attorney General v. Irish People, Inc.*, the court explained that, upon assertion of the state secrets privilege, "courts must balance a number of factors in determining how to proceed when one side or the other has claimed that certain evidence is privileged." 684 F.2d 928, 950-51 (D.C. Cir. 1982). The court acknowledged that "dismissal is not automatic," but it also made clear that it was "not asserting that dismissal is never proper in a civil context." *Id.* at 953 & n.144. The court held that

dismissal was inappropriate in that case because there was no showing that "the material which defendant seeks is relevant, let alone necessary, to the defense" and because "[t]here are . . . alternatives available to defendant, which will afford the information which would be useful to it at a civil trial, while not impairing the Government's legitimate interests." *Id.* at 954; *see also United States v. Koreh*, 144 F.R.D. 218, 223 (D.N.J. 1992) (concluding under *Irish People*'s "balancing approach" that Government's complaint should not be dismissed because privileged state secrets would "add[ ] little or nothing to the ammunition defendant [already] ha[d]" and because, as an alternative to dismissal, "Government ha[d] offered to stipulate to the information that the withheld documents would disclose"); *Republic of China v. National Union Fire Ins. Co.*, 142 F. Supp. 551, 557 (D. Md. 1956) (court declined to dismiss Government claim notwithstanding assertion of state secrets privilege because "necessity for the disclosure of the information requested [by the civil defendant was] dubious").

2. Proposed Federal Rule of Evidence 509(e) instructed that, if the Government's assertion of its state secrets privilege "deprived [the opposing party] of material evidence," the court should remedy the deprivation by "mak[ing] any further orders which the interests of justice require," including "dismissing the action." 56 F.R.D. 183, 252 (1972); *see* Boeing Br. 48-49.

Citing an Advisory Committee note, the Government suggests that the Contractors seek to use the assertion of the privilege "as an offensive weapon against" the Government. 56 F.R.D. at 254, *quoted in* U.S. Br. 46 n.15. To the contrary, the Contractors merely seek defensively to ensure the integrity of the proceedings under substantively and procedurally limited conditions: if the Government's assertion of privilege requires the Contractors to lay down their shield, the Government must lay down its sword.

3. Contrary to the Government's assertion, U.S. Br. 43-44, cases involving the privilege against self-incrimination have reached similar conclusions. *See* Boeing Br. 49-51. For example, although the court in *Serafino v. Hasbro, Inc.* rejected "automatic dismissal" as a constitutionally impermissible "penalty" upon a civil plaintiff's invocation of the self-incrimination privilege, it nevertheless approved of dismissal "as a *remedy* to prevent unfairness to the defendant" where "defendants would be substantially prejudiced" by the privilege and there was "no adequate alternative remedy to dismissal." 82 F.3d 515, 517-19 (1st Cir. 1996) (quotation marks omitted); *see also Wehling v. Columbia Broad. Sys.*, 608 F.2d 1084, 1087-88 & n.6 (5th Cir. 1979) (same).

Campbell v. Gerrans, cited by the Government, held only that the assertion of the self-incrimination "privilege in the discovery stage of a civil case cannot *automatically* be characterized as 'willful default' resulting in dismissal." 592 F.2d 1054, 1057-58 (9th Cir. 1979) (emphasis added), *cited in* U.S. Br. 44.

United States v. Certain Real Property and Premises Known as 4003-4005 5th Ave., 55 F.3d 78 (2d Cir. 1995), did not concern whether "a party's invocation of that privilege [can] justify dismissal of his claim," U.S. Br. 44, but rather whether a party's *withdrawal* of the privilege claim justified barring his testimony. In any event, the court prescribed consideration of "the precise facts and circumstances" to craft an "appropriate remedy for the assertion of the privilege." 55 F.3d at 84-85 (quotation marks omitted). And *Rhone-Poulenc Rorer Inc. v. Home Indemnity Co.* held only that "[r]elevance is not the standard" for determining whether the attorney-client privilege should be deemed waived. 32 F.3d 851, 864 (3d Cir. 1994), *cited in* U.S. Br. 43.

C. The Contractors Seek Only the Same Treatment the Government Demands for Itself.

The Government's brief in this Court is conspicuously silent as to its position on cases in which the assertion of the state secrets privilege substantially prejudices *the Government's own defense* against a civil claim. In fact, the Government has repeatedly and successfully argued that a private civil claim cannot proceed against it (or its affiliates) in such circumstances. *See* Boeing Br. 52-54. The Contractors ask only for the same rule that the Government insists upon when similarly situated. There is no

principled basis for the self-serving exemption from this rule urged by the Government here.[3]

1. Most fundamentally, the threat posed to the integrity of the judicial process when the assertion of the state secrets privilege substantially prejudices a party's ability to defend is certainly not less when the prejudiced party is a private actor rather than the Government. If anything, the threat is greater, and thus the need for procedural "protection is of particular importance," when the Government is the party both asserting the privilege and advancing a claim for affirmative relief, and thus "has a direct pecuniary interest in the outcome of the proceeding." *United States v. James Daniel Good Real Prop.*, 510 U.S. 43, 55-56 (1993).

2. The Government's sovereign immunity argument, *see* U.S. Br. 28, 35-36, fails because the Government is the moving party seeking affirmative relief on its default-termination claim. *See* Boeing Br. 41-42.

[3] The one-sided nature of the Government's position in civil cases is not mitigated by its concession that dismissal is appropriate when the state secrets privilege substantially prejudices a criminal defendant's ability to defend. *See* U.S. Br. 39-41. Indeed, permitting a criminal to go free will often pose a graver harm to the public than merely forgoing a civil claim. In all events, it is well settled that the principles of basic fairness and due process upon which the Contractors rely apply to civil as well as criminal defendants. *See* Boeing Br. 29-30, 35-38, 40-43; General Dynamics Reply 18-19.

3. None of the authorities cited by the Government establishes that the Contractors' proposed rule would impair the Government's ability to carry out immigration, counterterrorism, or intelligence programs. *See* U.S. Br. 41 n.13, 42. The programs referenced by the Government all permitted consideration of classified information ex parte and in camera. *See* 8 U.S.C. § 1189(a)(3)(B), (c)(2); *id.* § 1225(c)(2); *id.* § 1229a(b)(4), (c)(2); *id.* § 1534(e)(3); 18 U.S.C. § 2339B(f); *id.* § 3511(e); 50 U.S.C. § 1702(c); *id.* § 1806(f); 8 C.F.R. § 244.3 (1952). Because the Contractors were entirely foreclosed from litigating a prima facie valid defense and there is no adequate alternative remedy to dismissal, the Court need not decide whether due process allows the Government to press a claim while confining classified evidence to ex parte, in camera consideration. In any event, these programs would not be impaired by adoption of the rule proposed by the Contractors because they explicitly require that the classified information be disclosed to the private party if necessary to adjudicate the defense, 18 U.S.C. § 2339B(f)(2)(B); 50 U.S.C. § 1806(f), or involve persons having little or no due process rights, *Shaughnessy v. United States ex rel. Mezei*, 345 U.S. 206, 212-14 (1953); *Jay v. Boyd*, 351 U.S. 345, 358-59 (1956), or would plainly be undermined by the disclosure of classified evidence, *see, e.g.*, 8 U.S.C. § 1189 (designation of foreign terrorist organizations); *id.* § 1534 (alien terrorist removal); 18 U.S.C. § 2339B (prohibition of material support of foreign terrorist organizations); 50 U.S.C. §§ 1701-02 (emergency freeze of foreign assets); *id.* § 1806

(warrantless foreign intelligence surveillance); *see Global Relief Found., Inc. v. O'Neill*, 315 F.3d 748, 754 (7th Cir. 2002).

4. The Government fears, it says, that a ruling for the Contractors here would encourage contractors to "raise marginal or meritless superior-knowledge or other claims simply to induce the government to invoke the state-secrets privilege, thereby achieving automatic invalidation of a justified default termination." U.S. Br. 20. But under the Contractors' proposed rule, dismissal would be subject to the substantive and procedural limitations discussed above. Notably, the Government has not suggested, nor could it suggest, that the Contractors disingenuously asserted their superior-knowledge defense.

5. Finally, the Government's hypothesized "conflict" between its "duty . . . to safeguard national security" and its "responsibility to protect the public fisc," U.S. Br. 18, 26, 45-46, will rarely occur. As the many cases discussed in the briefs show, the rule advocated by the Contractors will almost always be invoked by *the Government as defendant* (or for the benefit of an affiliated defendant). In those cases, there is no conflict between the interests in securing the Nation's secrets and preserving the public fisc. In the few cases where the invocation of the state secrets privilege substantially prejudices a private party's ability to defend against a Government claim, it is entirely appropriate for the Government to bear the burden of protecting the Nation's secrets by forgoing its claim. In its brief to this Court in *Reynolds*, the

Government explained this point well: when it is the "plaintiff," the Government may fairly be put to the "choice of seeking the aid of the courts by pursuing the action," on the one hand, "or of refusing to produce" state secrets, on the other hand, for even if the Government "refuses to produce" and thus is "denied judicial assistance," "the public is left in no worse position than if [the Government] had never instituted the action." Br. for United States at 17, 66, 345 U.S. 1 (1953), *available at* 1952 WL 82378; *see* Boeing Br. 35-36.

♦

CONCLUSION

The judgment of the court of appeals should be reversed.

January 4, 2011

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v.
UNITED STATES OF AMERICA,
Respondent.

THE BOEING COMPANY,
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v.
UNITED STATES OF AMERICA,
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On Writ Of Certiorari To The
United States Court Of Appeals
For The Federal Circuit

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INTRODUCTION

The courts below upheld the government's default claim even though the state-secrets privilege barred the Contractors from litigating a *prima facie* valid defense. That result is fundamentally unfair, and the *Reynolds* rule forbids it. The government has long espoused that rule, and has often benefited from it. But here the government strives to evade it, both by contending that the Contractors are actually the moving parties as to the issue of default, and by insisting that the rule can never operate to disadvantage the government.

This Court should reject those arguments. First, as to the default claim, the government clearly is the moving party. It is asserting that the Contractors breached the contract and seeking to impose a drastic forfeiture. And it has the burden to prove that claim *de novo*, without reliance on the contracting officer's decision, which has no remaining legal force. The unique statutory procedure that forces the Contractors to appear as nominal "plaintiffs" does not alter those realities. Nor does the fact that the Contractors asserted in their complaint a separate claim for reimbursement of performance costs – a claim that would not even be ripe for litigation until after the government lost on its default claim.

Second, when the government is the moving party, it should not be granted special immunity from the operation of the *Reynolds* rule. Indeed, adherence to that rule is especially vital where the government can advance its own litigation interests

through invocation of the powerful state-secrets privilege.

The ruling below that the Contractors defaulted implicates the courts in the imposition of onerous penalties even though there is no way to know whether that outcome is justified on the merits. That ruling violates due process and undermines the integrity of the judicial system. It must be reversed.

ARGUMENT

I. The Government Is The Moving Party On Its Claim of Default.

The government alleged in the trial court that the Contractors breached the A-12 contract because they were not reasonably likely to meet their future obligations in a timely fashion. The government bore the burden of proof on that claim. *See Lisbon Contractors v. United States*, 828 F.2d 759, 764-65 (Fed. Cir. 1987). And although the government did not seek a court order directly imposing monetary or other penalties, it did seek a ruling that it had proved default – a determination the government *needed* before it could seek to impose sanctions on the Contractors using its asserted powers of offset and its control over future contract awards. The government received what it sought: a ruling that "the Government was justified in terminating the contract for default," Pet. App. 155a; *see also, e.g.*, *id.* at 28a, 174a, and a "judgment . . . in favor of" the government. JA1293; *see also* JA1262; *compare* Gov't Br. 29. The government got this relief even though the Contractors asserted a *prima facie* valid defense to the default claim that they were not

permitted to litigate. And in direct reliance on the Federal Circuit's affirmance of the judgment, the government demanded immediate payment of nearly $3 billion dollars. Dec. 29, 2009 Ltr. ("The recent appellate court action has affirmed and rendered final the trial court's judgment in the Government's favor. Accordingly, the Contractors' repayment . . . is due . . . ."). There is thus no doubt that the government was the moving party on its default claim.

A. The Government Was The Moving Party On Default Both When Its Contracting Officer Declared The Contractors In Default And When The Government Tried To Prove That Claim In Court.

The government was the moving party at the inception of the dispute over contract performance, and has retained that status at every subsequent stage.

1. Under the Contract Disputes Act ("CDA"), a government allegation of default is a government "claim." 41 U.S.C. § 605(a) (discussing "claims by the government against a contractor relating to a contract"). Any such claim is first addressed by the contracting officer, *see id.* – a highly partial decision-maker who represents the government's interests. Here, the contracting officer decided that the Contractors were in default and that the government was entitled to terminate the contract on that basis. As the trial court found, he also decided that the government was entitled to a specific amount of money as a result: more than $1 billion in

"unliquidated progress payments," plus interest. JA353-54.

The government suggests that payment of this amount would not be a forfeiture. But contrary to the government's assertion, the "unliquidated" payments were not for work that was never performed, Gov't Br. 37-38 – and certainly not, as the government insinuates, Gov't Br. 19, for work that was scheduled to be done sometime after the termination date. Rather, they were reimbursement for work that the Contractors actually carried out prior to termination, at the government's direction. JA111-15; *see also* Pet. App. 57a & n.12. Moreover, the payments did not even cover the Contractors' pre-termination costs of performance, which exceeded the total amount the government paid by over $1 billion. Accordingly, it is clear that the government was the moving party seeking to impose an enormous forfeiture on the Contractors. GD Br. 44 (collecting cases).[1]

[1] As for the "liquidated" progress payments, which the government suggests were a windfall, *e.g.*, Gov't Br. 50, those were final contract payments relating to design and engineering work that the government formally accepted. The government clearly is responsible for those costs. 48 C.F.R. § 52.249-9(f). Although the government did not "receive a single aircraft," Gov't Br 22, 50, that is because the government terminated the contract *nearly a full year* before any aircraft was due, Pet App. 71a. And as to non-monetary penalties, the government's assertion that they are not at issue, Gov't Br. 38, is misleading. If this Court upholds the default termination, the government remains free to impose them *See, e.g.*, 48 C.F.R §§ 9.103 to 9.105-1, 42.1500 to 1501.

2. The government retained its moving-party status when the matter moved to the Court of Federal Claims. A contracting officer's unilateral decision about a government claim of default becomes final and enforceable if a contractor does not exercise its right to have the government's claim decided instead by the Court of Federal Claims (or the Board of Contract Appeals). 41 U.S.C. § 605(b). But once a contractor indicates that it wants the government's claim to be adjudicated by a neutral arbiter, the officer's decision has no further effect. *See, e.g., Assurance Co. v. United States*, 813 F.2d 1202, 1206 (Fed. Cir. 1987) (holding that the "established rule" is that the filing of the suit "vacate[s]" the contracting officer's decision). The government must then proceed *de novo* to prove material breach. 41 U.S.C. §§ 605(a), 609(a) (providing that government can make a "claim[]" against a contractor at the contracting-officer stage, that "a contractor may bring an action directly *on the claim* in the United States Court of Federal Claims," and that court review is "de novo" and the contracting officer's findings "shall not be binding" (emphasis added)); *see also* 28 U.S.C. § 1491 (court has jurisdiction over "any [CDA] claim by *or against*, or dispute with, a contractor . . . , including a dispute concerning termination . . . ." (emphasis added)).

In this case, then, the government remained in the position of breach-of-contract claimant in the trial court. Under the statute, the suit is "on the [government's] claim" of default, not on the contracting officer's decision as to that claim. 41 U.S.C. §§ 605(a), 609(a). The government was

required to start anew, and the court had to decide whether the government had carried its burden. And the government was seeking affirmative relief from the court – a declaration that the government had proved default, without which the government could not seek the return of progress payments or impose other default penalties.[2]

B. The Government's Contrary Arguments Are Unavailing.

Given this statutory scheme, the Court should reject the government's strained arguments that the Contractors were somehow the moving parties on the default issue.

1. It is of no moment that the Contractors appeared as "plaintiffs" in the case caption. Gov't Br. 27. Application of the *Reynolds* rule cannot turn on that formalism.[3] Under the CDA, the Contractors' suit simply triggers the government's obligation to prove its default claim, and the case proceeds much like any breach-of-contract suit. *Lisbon*, 828 F.2d at 764-65; *see also, e.g.*, *Ameron Int'l Corp. v. Ins. Co. of Pa.*, 118 Cal. Rptr. 95, 105 (Cal. 2010) ("Although the

[2] The government may be able to hold claimed money while a case is pending (although it did not do so here), but that is simply an interim remedy, which can be unwound when the court ultimately rules. *See, e.g.*, *Seaboard Surety Co. v. United States*, 67 F. Supp. 969, 971 (Ct. Cl. 1946).

[3] Because the government can never appear as a plaintiff in the Court of Federal Claims, Gov't Br. 28, if that factor were controlling the government would never bear any burdens associated with an invocation of the state-secrets privilege in government-contract disputes. Such a rule would be grossly inequitable and likely to foster abuses. *See infra* pp. 19-20

contractor thus initiates the . . . proceeding [under the CDA], the purpose of the proceeding is to resolve the claim against the contractor, who is therefore in the position of a defendant.").[4]

2. Despite the government's frequent references to the Contractors' superior-knowledge "claim," superior knowledge operated only as a *defense* to the government's claim of default. It is a reason why the government was not entitled to terminate the contract for delay, which was the sole basis on which the courts ultimately upheld the default termination. *See* GD Br. 44 (government descriptions of Contractors' "defense"); *infra* note 5 (discussing superior-knowledge argument in context of the Contractors' contingent claim for incurred costs).

The government tries to separate its default claim from the Contractors' superior-knowledge defense, asserting that it is entitled to relief because it proved the elements of its claim without resort to privileged information. *E.g.*, Gov't Br. 32-33. But a claim and a defense to that claim are inextricably intertwined. The government cannot be said to have established its claim unless it has also overcome any defenses that could defeat the claim. That is why *Reynolds* mandated an end to any prosecution in which a

[4] This point is driven home by the fact that the Boards of Contract Appeals – the other neutral fora to which contractors can take a dispute, *see* 41 U.S.C § 607(d) – sometimes order the government to submit the first pleading, once a contractor has invoked their jurisdiction. *See, e.g., In re RO.VI B.Srl*, A.S.B.C.A. No. 56,198, 09-1 BCA ¶ 34,068, at 168,456 ("[T]he Board asked the government to file the initial pleading since default termination is considered a government claim.").

meaningful defense is stripped away, *United States v. Reynolds*, 345 U.S. 1, 12 (1953), and why the same result must obtain in this case.

The Contractors do bear the burden of proof as to their affirmative defense. Gov't Br. 35. But so, of course, does a criminal defendant – and the government concedes that a prosecution cannot go forward where a defense is taken away in the criminal context. *Id.* at 40; *see also id.* at 33 (it is improper to "fractur[e] the various issues" relating to a single claim to determine moving-party status); GD Br. 37-39 (explaining the uniform rule, endorsed by the government, that precluding an affirmative defense requires judgment against the claimant). The key fact is that the government had the duty of prosecuting the default claim as a whole; if both parties had failed to submit any evidence to the trial court, the Contractors would have prevailed. The government was the moving party, seeking to change the status quo and impose a forfeiture.

3. It also does not matter that the government did not ask the court to award the money it seeks or to impose any other specific default sanction. Gov't Br. 29. The government's claimed authority to inflict these penalties through self-help depends on having succeeded on its default claim in court, since the Contractors exercised their right to have the default issue judicially determined.

Congress designed the CDA dispute-resolution process to guarantee contractors a neutral forum for assessment of default. GD Br. 46 & n.10; *see also* 41 U.S.C. § 609(a)(1) (preserving right to suit

"notwithstanding any contract provision, regulation, or rule of law to the contrary"). Any other regime would be a violation of due process, giving the government free rein to impose monetary and other penalties without giving contractors a full opportunity to defend themselves. Here, the contract expressly guarantees the Contractors the right to have disputes heard and decided according to the requirements of the CDA, which are in any event necessarily implied into the parties' agreement. 48 C.F.R. § 52.233-1; 11 Williston on Contracts § 30:19, at 203-04 (4th ed. 1999).

Because under the CDA the suit deprived the contracting officer's decision of any force, the government repeatedly asked the courts below to judicially establish default. *See, e.g.*, Gov't Mot. S.J. at 89 (Fed. Cl. Dec. 22, 2003) ("[W]e respectfully request that the Court sustain the default termination, enter judgment in favor of [the government], and grant . . . such other and further relief as this Court deems just."); JA1285 ("Our burden below was to establish our claim of default."). It follows that the government was a moving party calling on the courts' aid – and they erroneously responded by granting that aid even though they could not determine whether it was legally and factually justified.

4. The government tries to analogize this case to a run-of-the-mill judicial challenge to administrative action, Gov't Br. 29-30, 38, but that comparison is misplaced. In an APA case, review is on an administrative record and is limited to the agency's stated reasons; some process has already been

provided at the administrative level; and, for that reason, review is deferential, such that the agency action remains an established fact unless the challenger can displace it. Here, by contrast, the government was free to come up with any reason at all to justify default, even if the contracting officer never considered it, GD Br. 43 n.9; there was no process afforded by the contracting officer; and there was no judicial deference due to the contracting officer's decision. Indeed, the Contractors' suit was "an action directly *on the [government's] claim*" of default as it was presented to the contracting officer, not an action for review of the contracting officer's decision. 41 U.S.C. §§ 605(a), 609(a) (emphasis added).

Accordingly, regardless of the rule that applies to ordinary APA review, here the government was the moving party on its default claim, litigating for the right to extract relief from the Contractors. In so doing, it was seeking to change the status quo because, once the complaint was filed, the contracting officer's administrative determination effectively disappeared. The reasons that underlie the *Reynolds* rule are thus fully applicable here. Once the government's invocation of the state-secrets privilege barred a substantial defense, permitting the government to obtain affirmative relief allowed the government to manipulate the system and made the courts an instrument of injustice.

5. Although the government emphasizes *Reynolds*' reference to a suit "only on terms to which [the government] has consented," 345 U.S. at 12, *cited in* Gov't Br. 35-36, that language has no

significance for purposes of the government's default claim. The Court was not referring there to a case in which the government is only a nominal defendant and is pursuing its own claim. It was referring to the government's defense against a claim for affirmative relief brought by someone else (as in *Reynolds* itself). Only then might sovereign immunity be a relevant consideration. *See infra* pp. 18-19.

6. Finally, none of this analysis is changed by the fact that the Contractors also raised their own claim for recovery of unreimbursed costs incurred in performing the contract. *E.g.*, Gov't Br. 28-29. The Contractors' claim, which was the subject of a separate contracting officer decision from the default claim and arises only if the government's default claim is first rejected, *McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 285, 287-91 (1997), in no way undercuts the point that the government cannot prevail as a moving party on default once its assertion of the state-secrets privilege has eliminated the Contractors' defense. Plainly, moving-party status must be assessed on a claim-by-claim basis. Whether or not the Contractors should be allowed to pursue their own claim once the default is overturned,[5] the government was the moving party

[5] After it initially rejected the government's default claim on the merits, the trial court awarded the Contractors their out-of-pocket costs – but not profit, as to which they would have been required to prevail on the superior-knowledge issue. The government contends that the court should have refused to award any costs, on the ground that the state-secrets privilege prevented full consideration of all issues relating to the Contractors' cost claim. Gov't Br. 54 n.21 The government's argument is wrong. The Contractors' claim is distinct in kind

as to *its* own claim – a conclusion that requires reversal of the Federal Circuit's decision.

II. Because The Government Is The Moving Party, It Should Not Have Been Permitted To Pursue The Default Termination Once The Privilege Barred A Substantial Defense.

A. There Is No Special Government Exception to the *Reynolds* Rule.

The government acknowledges the basic soundness of the rule that the moving party may not prevail on a claim if the state-secrets privilege wipes out a substantial defense. Gov't Br. 25-27. But it tries to justify a government-only exception that it intends to use to extract nearly three billion dollars from the Contractors. These arguments are based on two false premises. First, the government erects a strawman, claiming that the Contractors are seeking an "automatic" rule under which the government necessarily loses if it invokes the state-secrets privilege. Second, the government suggests that if the Contractors prevail it will somehow have been "punished" for asserting the privilege, arguing that the government should win regardless of the unfairness to the other party. But the Contractors are not saying that the government should always lose if it invokes the privilege – and neither should the government always avoid the burdens associated

from the default claim – and the government's "loss ratio" argument, *see id.*, is itself a claim, not a precluded defense. 48 C.F.R. § 49.203(a). Of course, if the government were correct, the result would be that *all* claims are barred, such that neither party may recover anything from the other.

with such an invocation. Rather, the Court should rule that *no* moving party can proceed with a claim for relief if the privilege entirely prevents litigation of a significant defense. Under that rule, the default termination cannot be sustained.

1. The Contractors do not argue that they should prevail simply because the government invoked the state-secrets privilege while it was the moving party. *E.g.*, Gov't Br. 26, 39, 41. Such an outcome is appropriate only in "exceptional cases," GD Br. 33 – those in which the non-moving party raises a *substantial* defense and the court cannot fashion a procedural solution that will allow the defense to be considered while still protecting the Nation's secrets.

In most cases, the state-secrets privilege will not operate to strip a party of a defense. More typically, the privilege simply makes certain evidence unavailable, or the court can use various procedures to minimize the risk of dangerous disclosure – or even review the secret evidence itself and assess which side that evidence would favor. *E.g.*, *Molerio v. FBI*, 749 F.2d 815, 825 (D.C. Cir. 1984). In addition, in most cases, a party will not be able to come forward with sufficient non-secret evidence to establish that its defense is substantial, so as to assure the court that deprivation of the defense may work an injustice. For instance, in the three cases the government cites in which it invoked the state-secrets privilege as a moving party and was nevertheless permitted to proceed, the courts specifically determined that the secret evidence was so unlikely to be helpful to any defense that there was no danger of unfairness. Gov't Br. 42.

This case is entirely different. The government does not meaningfully contest the trial court's determination that the Contractors had a *prima facie* valid superior-knowledge defense, which was barred only after years of struggle to find a way to allow its substantive resolution. To be sure, the government seeds its brief with factual assertions intended to suggest that the Contractors had all the information they needed, or that they disregarded government warnings. *E.g.*, Gov't Br. 1-3. But these assertions are misleading at best,[6] and certainly do not cast doubt on the trial court's repeated conclusions, based on its familiarity with the voluminous record, that the Contractors had a substantial superior-knowledge argument and might well have defeated the government's default claim if they had been permitted to put on their evidence. The trial court never retreated from those conclusions – it said that it could not definitively determine who would prevail

[6] For example, the government's claim that the Navy's sharing of a pre-award weight estimate constituted a "general warning," Gov't Br. 3, 52, ignores the facts. The government provided – without useful explanation – a design weight estimate that differed from the Contractors' final proposed weight by an inconsequential amount. Despite the government's superior knowledge from other programs and from Northrop's competing bid, the estimate gave the Contractors no indication that their approach would result in a much higher design weight and require extensive redesign work. Trial Transcript Vol. II at 613, Nov. 28, 1995; Gov't Ex 5050 at 9; JA1083-85 The Contractors then spent months and many millions of dollars attempting to meet the weight "guarantee" – which the Navy ultimately waived, Pet. App. 239a, 388a – without benefit of vital information possessed by the government. Pet App. 416a; *see also* JA648, 670-74, GD Br. 3-5; Pls.' Memo. at 3-9 (Fed. Cl. Feb. 1, 1994).

if the defense went to trial, Pet. App. 245a, *cited in* Gov't Br. 16 n.8, but its opinion about the strength of the Contractors' evidentiary showing remained unchanged, GD Br. 54-55.

Given the rarity of cases like this one, "graymail" is hardly a meaningful issue. Gov't Br. 26-27. Any real "graymail" concern arises with trumped-up claims *against* the government, not *defenses* to government claims. *See id.* But, in any event, under the regime developed by the courts of appeals, no party can realistically hope to prevail by manufacturing a defense that might implicate state secrets, because there is a high likelihood that the defense will be deemed insufficiently substantial (or that there will be some other obstacle to applying the *Reynolds* rule).[7]

2. Nor should the Court take seriously the argument that a ruling against the government would be tantamount to a "punish[ment] for asserting the privilege." *E.g.*, Gov't Br. 45-46. To begin with, the government concedes that the *Reynolds* rule applies in criminal cases, in which the government must choose whether it wants to insist on the privilege or proceed with a prosecution. Gov't Br. 39-40 (citing *Jencks*). There is no more "punishment" involved when the government is put to this choice in the civil context.

[7] Given the limited reach of the *Reynolds* rule, it is not surprising that proposed Rule of Evidence 509 listed dismissal as only one possible option. *Proposed Rules*, 56 F.R.D. 183, 251-52 (1972); *see also* GD Br. 34 n.6 (discussing similar CIPA provision), *compare* Gov't Br. 46 n.15

The Contractors are simply asking that the government be treated the same as any other litigant, bearing a burden as a result of a privilege assertion only where it is the moving party and only where a substantial defense has been prevented from being asserted. *Compare Salisbury v. United States*, 690 F.2d 966, 975 (D.C. Cir. 1982), *cited in* Gov't Br. 27, 46, 50. It is surprising that the government would suggest the viability of any exception to the operation of the *Reynolds* rule in those circumstances, since the government benefits from the rule much more often than it is burdened. Moreover, where the government as moving party does determine that the "collective public interest" in secrecy is "paramount," Gov't Br. 46, the potential loss of an *affirmative* civil claim will not create undue pressure to change that determination. GD Br. 30 n.4, 34 n.6. The government should not be permitted to force a particular private party to suffer a penalty on behalf of the collective – particularly here, where even the worst possible outcome for the government includes no penalties for its decision to end the contract. GD Br. 6-7.

3. The government argues that if it is subject to the *Reynolds* rule when it is a moving party it will not be able to carry out certain statutory mandates, which envision that the government will bring suit in the interests of national security. Gov't Br. 42-43. But the *very statutes* the government cites illustrate that Congress envisioned that the government would be subject to the *Reynolds* rule when it is the moving party in a civil action. For instance, 18 U.S.C. § 2339B, which contemplates a civil suit for an

injunction, bars the government from keeping classified material out of the record without providing a substitute (such as a stipulation) "sufficient to allow the defendant to prepare a defense." *Id.* § 2339B(f)(2); *see also* 18 U.S.C. § 3511 (requiring the district court to review classified information *in camera* if the government wishes to protect it from general disclosure). Thus, there is no danger that a ruling in favor of the Contractors will do anything to prevent the government from proceeding as Congress intended.

4. The government suggests it is not a matter of great import to disregard the *Reynolds* rule in the civil context. Gov't Br. 40-41. But it is just as improper in a civil case as in a criminal one for a court to order affirmative relief when it cannot determine which side should prevail. Indeed, this Court's prior rulings make clear the serious due process concerns raised when invocation of the privilege prevents a civil party from offering a defense using non-secret information already in its possession. GD Br. 30 (collecting cases).[8]

[8] In this way, the state-secrets privilege is different from other evidentiary privileges – it alone makes *entire issues* incapable of litigation, even if the relevant evidence is not itself privileged and is in the hands of the party that wants to present it. *Compare Rhone-Poulenc Rorer Inc. v. Home Indem. Co.*, 32 F.3d 851, 864 (3d Cir 1994) ("[O]ur holding is not meant to preclude disclosure of the knowledge the insureds possessed."), *cited in* Gov't Br. 43-46. The immigration cases cited by the government, Gov't Br. 41 n.13, do not establish that due process protections are inapplicable in that circumstance. Indeed, the primary case on which the government relies, *Shaughnessy v. United States ex rel. Mezei*, 345 U.S. 206 (1953), rested on the

Notably, the government is not willing to subject *itself* to such a regime. It would bar operation of the *Reynolds* rule in the civil context only when the government is the moving party, while preserving its own right to invoke the rule when the privilege blocks a government defense in a civil case. Gov't Br. 40-41. But the government's arguments for the civil/criminal distinction do not support such a limited bar. If taken seriously, they would mean that the government as defendant could not obtain a judgment in its favor where it is deprived of a defense, and neither could a private defendant sued by a private plaintiff. Yet these are both situations in which the government has long successfully advocated for application of the *Reynolds* rule. GD Br. 38-39. In reality, the proposed civil/criminal distinction is just another way of arguing that the government should be specially immunized from suffering any burden as a result of the uniquely powerful privilege it controls.

5. Finally, sovereign immunity presents no barrier here. The government can suggest otherwise only by conflating its own claim for default and the Contractors' separate and contingent claim for a termination-for-convenience cost recovery. Gov't Br. 28, 35-36; *see supra* pp. 10-11. As to the government's affirmative request that the courts find the Contractors in default, sovereign immunity is irrelevant. *Cf. Lapides v. Bd. of Regents*, 535 U.S. 613, 619-20, 622 (2002) (immunity cannot be wielded as a sword). And even if waiver of sovereign

holding that aliens who have not entered the United States have *no due process rights*. *Id.* at 212.

immunity were somehow made relevant by the unusual procedures though which the government's default claim comes to court, the applicable waiver is more than adequately broad. It covers all matters relating to a government contract, *see* 28 U.S.C. § 1491(a)(1)-(2), with no "limitations" or "conditions," *Soriano v. United States*, 352 U.S. 270, 276 (1957); *see United States v. Mitchell*, 463 U.S. 206, 215 (1983) (waiver of contract-dispute immunity is "perhaps the widest and most unequivocal waiver of federal immunity").

6. Since the government is entitled to no special shield, it should be subject to the same rule for which it has so frequently advocated when it is in the position of a defending party rather than a moving one. GD Br. 38-39. Indeed, the government's request for unique protections disregards the realities of litigation. The need for the rule is *more* acute where the government is the moving party, not less so, because the government has every incentive to ensure a favorable outcome for itself, *see Reynolds*, 345 U.S. at 12 – particularly where, as here, the potential reward for doing so is high. The government protests that it can be trusted and would never act in anything but the most upright fashion. Gov't Br. 47-49. But that cannot be squared with the government's candid acknowledgement that its officials are influenced by financial considerations. Gov't Br. 26, 47. Nor can it be reconciled with the government's record of misconduct in litigating this case after the privilege was invoked. GD Br. 32-33. The government barely addresses the trial court's

repeated expressions of concern about its conduct,[9] but the record well illustrates the risk that the government will act aggressively if its use of the privilege has no conceivable downside.

The "government always wins" rule also disregards the realities of government contracting. As the industry amicus brief makes clear, NDIA Br. 2, 11-17, announcement of such a rule by this Court would have a chilling effect on contractors contemplating complex or high-risk contracts, who would never know in advance whether their case will be the one in which a valid defense cannot be litigated. The government's proposed solution – that contractors should negotiate for contract terms protecting against that eventuality, Gov't Br. 51 – is no answer. Contractors have no bargaining power to vary mandatory contract terms such as the standard "Disputes" clause. *See, e.g., United States v. Seckinger*, 397 U.S. 203, 212 (1970) ("there is a vast

[9] In an April 1993 decision, the Federal Circuit stated that the submissions before it did not establish that the government had used privileged information for "tactical purposes." JA568 n.5, *cited in* Gov't Br. 48 n.17. But that decision obviously did not address the trial court's many *subsequent* findings about government bad acts that preceded and followed that date. For example, the trial court later found that the government had improperly used privileged information to ask "highly inappropriate, leading follow-up questions designed to elicit responses that would benefit" the government – conduct that required "extraordinary corrective action" and led to sanctions on government attorneys. Pet. App. 357a-60a & nn.9-10, 433a n.1; JA550-51. The Circuit also did not address the government's frequent changes of position on whether the case could be litigated after invocation of the privilege, all designed to further its own interests. GD Br. 13-14, 16, 39, 50 n.13.

disparity in bargaining power and economic resources between . . . the United States and particular government contractors"); *Sandnes' Sons, Inc. v. United States*, 462 F.2d 1388, 1392 (Ct. Cl. 1972) ("Government contracts are contracts of adhesion"); *Do-Well Mach. Shop, Inc. v. United States*, 870 F.2d 637, 641 (Fed. Cir. 1989) (government has "superior bargaining power"); *Appeal of Penner*, G.S.B.C.A. No. 6820-R, 83-1 BCA ¶ 16,495, at 81,987 (clause in a government contract is "every bit as unilateral an enactment on the part of the Government" as a statute).[10]

B. The Government Can No Longer Rely On The Contracting Officer's Decision, And Judgment Should Be Entered For The Contractors On The Issue Of Default.

In addition to arguing that the *Reynolds* rule should not apply here, the government also seems to suggest that the proper outcome, if the rule applies, would be a dismissal leaving the contracting officer's default determination in place. Gov't Br. 32 n.9, 34. This Court should firmly reject any such notion.

The filing of the Contractors' suit meant that the government had to prove its default case from scratch. Because the *Reynolds* rule precludes the courts from holding that the government has carried its burden on that question, the government cannot

[10] The suggestion that government might voluntarily agree to subject itself to the *Reynolds* rule, if taken seriously, undercuts the force of the government's arguments about why it needs to be able to impose defaults on contractors deprived of their defenses.

prevail. It cannot continue to claim the right to penalize the Contractors by insisting that the contracting officer's unilateral decision retains some vitality. That would not only deny the Contractors due process but also contravene the CDA and the parties' contract. *See supra* pp. 8-9.

For these reasons, application of the *Reynolds* rule cannot justify pretending that this lawsuit was never filed and that the contracting officer's decision therefore became enforceable by operation of law. Rather, the effect of the rule is that the contract remains terminated, but the government as moving party cannot claim to have established default and thus cannot seek to impose default sanctions.[11] Otherwise, the government would win even though it never proved its claim (a task that includes defeating any substantial defenses), and the courts would implicate themselves in the government's unfair imposition of a massive forfeiture.[12]

[11] *See* 48 C.F.R. § 52.249-9(g) Whether the Contractors are entitled to a termination-for-convenience cost recovery, as the trial court found, or the parties should instead walk away with no one recovering anything, is a further question. *See supra* note 5

[12] Petitioner does not agree that a remand is necessary to decide legal issues relating to the superior-knowledge defense. Gov't Br. 52-54. It is contrary to all existing precedent to suggest that a contractor who is to be trusted with developing highly sensitive technology should be deprived of information about that very technology, or even a warning about the infeasibility of proposed contract terms, based on an asserted need for secrecy. *See* GD Br. 56 & n.14 (citing *J.A. Jones Constr. Co. v. United States*, 390 F.2d 886 (Ct. Cl. 1968)); *see also United States v. Speed*, 75 U.S. 77, 84 (1868); *Bannum, Inc. v. United States*, 80 Fed. Cl. 239, 247 (2008). Moreover, the government

CONCLUSION

For the foregoing reasons, this Court should reverse the Federal Circuit's ruling upholding default.

Respectfully submitted,

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expressly promised to provide critical stealth information to the Contractors, and those promises were a premise of the Navy's decision to undertake the program and of the contracting relationship. GD Br. 3-5; *see also, e.g.*, May 26, 1993 Appendix at Tab 7, JA646-47, 658-59, 687. If the Court nevertheless decides to remand for consideration of these issues, it should ensure that the government's continued reliance on the contracting officer's decision is foreclosed, and that the Federal Circuit's task is clearly circumscribed.

AMICUS CURIAE BRIEF

Supreme Court, U.S.
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Supreme Court of the United States

GENERAL DYNAMICS CORPORATION,

Petitioner,

v.

UNITED STATES,

Respondent.

THE BOEING COMPANY, SUCCESSOR TO MCDONNELL DOUGLAS CORPORATION,

Petitioner,

v.

UNITED STATES,

Respondent.

On Writs Of Certiorari To The United States Court Of Appeals For The Federal Circuit

BRIEF FOR AL-HARAMAIN ISLAMIC FOUNDATION, INC., WENDELL BELEW, ASIM GHAFOOR, AND ELECTRONIC FRONTIER FOUNDATION AS AMICI CURIAE IN SUPPORT OF NEITHER PARTY

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BRIEF FOR AL-HARAMAIN ISLAMIC FOUNDATION, INC., WENDELL BELEW, ASIM GHAFOOR, AND ELECTRONIC FRONTIER FOUNDATION AS AMICI CURIAE

INTRODUCTION

Amici curiae Al-Haramain Islamic Foundation, Inc., Wendell Belew, Asim Ghafoor, and the Electronic Frontier Foundation file this brief to address an issue the government has raised in opposition to certiorari in these consolidated cases and in a previous case before this Court: whether the state-secrets privilege has a constitutional basis in Article II. That issue is not presented here, and thus the Court should not address it. If the Court chooses to do so, however, the Court should conclude that the state-secrets privilege is a common-law evidentiary rule of nonconstitutional provenance.[1]

♦

INTEREST OF AMICI CURIAE

1. *The Al-Haramain Amici Curiae.* Amici curiae Al-Haramain Islamic Foundation, Inc., Wendell Belew, and Asim Ghafoor are the plaintiffs in *Al-Haramain Islamic Foundation, Inc. v. Obama*, No.

[1] No counsel for a party authored this brief in whole or in part, nor did any person or entity, other than amici curiae or their counsel, make a monetary contribution to the preparation or submission of this brief. The consent of the parties to the filing of amici curiae briefs has been obtained and filed with the Clerk of the Court.

C-07-0109 (N.D. Cal. filed February 28, 2006), which awaits the district court's rendition of final judgment following a summary judgment of liability against the President of the United States, the National Security Agency, the Office of Foreign Assets Control, and the Federal Bureau of Investigation for warrantless electronic surveillance in violation of the Foreign Intelligence Surveillance Act (FISA), 50 U.S.C. §§ 1801-1810. *See In re National Security Agency Telecommunications Records Litigation*, 700 F. Supp. 2d 1182 (N.D. Cal. 2010).

Prior to adjudicating liability, the district court in the *Al-Haramain* case ruled that "FISA preempts or displaces the state secrets privilege . . . in cases within the reach of its provisions." *In re National Security Agency Telecommunications Records Litigation*, 564 F. Supp. 2d 1109, 1124 (N.D. Cal. 2008). In reaching that conclusion, the district court rejected the defendants' argument that the state-secrets privilege has a constitutional basis in Article II.[2]

[2] The *Al-Haramain* defendants' argument that the state-secrets privilege has a constitutional provenance was pertinent to determining the standard for deciding the preemption issue in that case. A federal statutory scheme preempts federal common law, even without explicit evidence of a clear and manifest purpose to do so, if Congress has "occupied the field through the establishment of a comprehensive regulatory program." *Milwaukee v. Illinois*, 451 U.S. 304, 316-17 (1981). In the *Al-Haramain* case, the defendants unsuccessfully argued "that the [state-secrets] privilege derives, not only from the common law, but also from the [P]resident's Article II powers, so that a 'clear

(Continued on following page)

Amici curiae anticipate that, if the *Al-Haramain* defendants choose to appeal the yet-to-be-rendered final judgment in that case, one of the questions presented on the appeal will be whether the state-secrets privilege has a constitutional basis in Article II. Amici curiae likewise anticipate that, in the present consolidated cases, the United States will argue in its merits briefing, as it did in opposition to certiorari, that the state-secrets privilege has a constitutional basis in Article II. If the Court's opinion includes a dictum addressing this question, it could affect the Ninth Circuit's decision of an appeal (if there is one) in the *Al-Haramain* case.

2. *Amicus Curiae Electronic Frontier Foundation.* The Electronic Frontier Foundation (EFF) is a non-profit, member-supported civil liberties organization working to protect rights in the digital world. Founded in 1990, EFF is based in San Francisco. EFF has more than 14,000 dues-paying members throughout the United States and around the world.

EFF serves as counsel in two cases arising out of the warrantless domestic dragnet surveillance conducted by the National Security Agency together with AT&T. In those cases, the Executive has asserted that the state-secrets privilege is a constitutionally-compelled rule which bars the Judiciary from

expression' of congressional intent is required to abrogate that privilege. . . ." *National Security Agency Telecommunications Records Litigation*, 564 F. Supp. 2d at 1120.

adjudicating the lawfulness of the Executive's actions under the Constitution and under federal statute. Those two cases are currently pending in the Ninth Circuit. *Hepting v. AT&T*, No. 09-16676 (9th Cir.); *Jewel v. NSA*, No. 10-15616 (9th Cir.). Any dictum here addressing the constitutional question of whether the state-secrets privilege is an Article II limitation on the power of the courts could affect those cases.

♦

SUMMARY OF ARGUMENT

Despite repeated invitations from the government in opposing certiorari in these consolidated cases and in the government's brief in a previous case, *Mohawk Industries, Inc. v. Carpenter*, 130 S.Ct. 599 (2009), this Court need not and should not here address the issue of whether the state-secrets privilege has a constitutional basis. The resolution of that issue is not necessary to these cases' adjudication and is outside the scope of the question on which the Court has granted certiorari. If and when the Court addresses this issue, the Court should do so only after full, direct briefing in a case where the issue is squarely presented and not in a dictum here.

If, however, the Court does address in these cases the provenance of the state-secrets privilege, the Court should conclude, consistent with the majority view among the lower federal courts, that

the state-secrets privilege is a common-law evidentiary rule of nonconstitutional provenance.

♦

ARGUMENT

I. THE COURT NEED NOT ADDRESS THE ISSUE OF WHETHER THE STATE-SECRETS PRIVILEGE HAS A CONSTITUTIONAL BASIS.

In the present consolidated cases, neither the Court of Federal Claims nor the Court of Appeals for the Federal Circuit addressed the issue of whether the state-secrets privilege has a constitutional basis in Article II. *See McDonnell Douglas Corp. v. United States*, 567 F.3d 1340, 1345 (2009); *McDonnell Douglas Corp. v. United States*, 323 F.3d 1006, 1020-24 (Fed. Cir. 2003); *McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 270, 278-81 (1996). Nevertheless, the United States has raised this issue in its opposition to certiorari, asserting that "[t]he state secrets privilege is deeply rooted in both 'the law of evidence,' *United States v. Reynolds*, 345 U.S. 1, 6-7 (1953), and the Executive's 'Art[icle] II duties' to protect 'military or diplomatic secrets,' *United States v. Nixon*, 418 U.S. 683, 710 (1974)." Brief for the United States in Opposition to Petitions for Writ of Certiorari at 12. Amici curiae anticipate that the United States may do so again in its merits briefing.

The resolution of this issue, however, is not necessary to the adjudication of the question on

which the Court has granted certiorari: whether the Due Process Clause of the Fifth Amendment permits the government to maintain a claim while simultaneously asserting the state-secrets privilege to bar presentation of a prima facie valid defense to that claim.[3] *See* Sup. Ct. R. 14(1)(a) ("Only the questions set out in the petition, or fairly included therein, will be considered by the Court."); Sup. Ct. R. 24(1) & (2) (briefs on merits may not raise additional questions or change the substance of the questions presented). The extent of Fifth Amendment due process rights is determined by balancing "the governmental and private interests that are affected," *Mathews v. Eldridge*, 424 U.S. 319, 334 (1976), whether or not the governmental interest is constitutional in origin. This Court has applied the balancing test in both situations. *See Hamdi v. Rumsfeld*, 542 U.S. 507, 527-31 (2004) (employing *Mathews* balancing test where government invoked constitutional war power to justify indefinite detention of enemy combatant); *id.* at 529 (*Mathews* test determines the process due "in any given instance"); *Roviaro v. United States*, 353 U.S. 53, 62 (1957) (prescribing balancing test to determine scope of nonconstitutional informer's privilege).

[3] Nor do these cases present the question of whether or to what extent the government may invoke the state-secrets privilege to defeat a constitutional claim against the government.

Thus, amici curiae urge the Court not to address the provenance of the state-secrets privilege in a dictum here. Any pronouncement by this Court on the provenance of the state-secrets privilege should await a case presenting that issue, upon full briefing by the parties. *See United States v. U.S. Gypsum Co.*, 333 U.S. 364, 411 (1948) (Frankfurter, J., concurring) ("Deliberate dicta . . . should be deliberately avoided.").

In *Mohawk Industries, Inc. v. Carpenter*, 130 S.Ct. 599 (2009), where this Court held that disclosure orders adverse to the attorney-client privilege do not qualify for immediate appeal under the collateral order doctrine, the United States submitted an amicus curiae brief which discussed the question – irrelevant in that case – whether the state-secrets privilege has a constitutional basis. *See* Brief for the United States as Amicus Curiae Supporting Respondent at 28-29, *Mohawk Industries, Inc. v. Carpenter*, 130 S.Ct. 599 (2009) (No. 08-678), 2009 WL 2028902 (arguing that the state-secrets privilege has constitutional grounding and performs a function of constitutional significance). The Court wisely refrained from including in its opinion any dictum addressing that question. The Court should do the same here.

If, however, the Court decides in these consolidated cases to address the provenance of the state-secrets privilege, the Court should conclude, for the reasons set forth below, that the state-secrets privilege is a common-law evidentiary privilege without foundation in the Constitution.

II. THE STATE-SECRETS PRIVILEGE IS A COMMON-LAW EVIDENTIARY RULE OF NONCONSTITUTIONAL PROVENANCE.

A. The State-Secrets Privilege is an Evidentiary Rule Rooted in the Common Law of England and Scotland.

The common-law provenance of the state-secrets privilege embodied in *United States v. Reynolds*, 345 U.S. 1 (1953) is described in two recent scholarly publications: William G. Weaver & Robert M. Pallitto, *State Secrets and Executive Power*, 120 POL. SCI. Q. 85, 92-101 (2005); and Robert M. Chesney, *State Secrets and the Limits of National Security Litigation*, 75 GEO. WASH. L. REV. 1249, 1270-80 (2007).

Weaver and Pallitto explain that "[t]he state secrets privilege derives from crown privilege as it developed in the common law of England and Scotland." Weaver & Pallitto, *supra*, 120 POL. SCI. Q. at 97. Chesney describes an early example of the privilege's common-law provenance: the 1817 decision in *Rex v. Watson*, a prosecution for "an alleged plot . . . to overthrow the British government through a series of acts that would include an assault on the Tower of London," where the court excluded testimony by a tower employee attesting to the accuracy of a map of the tower because "'it might be attended with public mischief, to allow an officer of the tower to be examined as to the accuracy of such a plan.'" Chesney, *supra*, 75 GEO. WASH. L. REV. at 1274-75 (quoting *Rex v. Watson*, 171 Eng. Rep. 591, 604 (K.B. 1817)). Weaver and Pallitto describe another early example:

the 1860 decision in *Beatson v. Skene*, where it was said:

> "[I]f the production of a state paper would be injurious to the public service, the general public interest must be considered paramount to the individual interest of a suitor in a court of justice. . . . It appears to us . . . that the question, whether the production of the documents would be injurious to the public service, must be determined not by the judge but by the head of the department having the custody of the paper."

Weaver & Pallitto, *supra*, 120 POL. SCI. Q. at 97-98 (quoting *Beatson v. Skene*, 5 Hurlst. & N. 838, 853 (1860)).

According to Weaver and Pallito, "the chief modern case on the issue of crown privilege" in the United Kingdom is the 1942 decision in *Duncan v. Cammel, Laird and Co., Ltd.*, in which "family members of submariners killed while putting the submarine Thetis through trials sued the manufacturer of the submarine and sought discovery of blueprints of the craft and other sensitive documents," but "[t]he Crown asserted privilege to protect the documents, and the Lords held that 'the approved practice . . . is to treat ministerial objections taken in proper form as conclusive.'" Weaver & Pallitto, *supra*, 120 POL. SCI. Q. at 98 (quoting *Duncan v. Cammel, Laird and Co., Ltd.*, [1942] A.C. 624, 641 (1942)). "The holding of *Duncan* conferred absolute authority on the executive

to withhold documents from disclosure in judicial proceedings." *Id.*

This Court's seminal decision in *Reynolds* on the state-secrets privilege relied largely on *Duncan* to prescribe the contours of the privilege. *See Reynolds*, 345 U.S. at 7-8. The Court explained that, while "[j]udicial experience with the privilege which protects military and state secrets has been limited in this country[,] English experience has been more extensive. . . ." *Id.* at 7. The Court cited *Duncan* as authority for several propositions: that invocation of the privilege requires "actual personal consideration" by the head of the department that has control over the matter, that "[t]he court itself must determine whether the circumstances are appropriate for the claim of privilege," and that the court must "do so without forcing a disclosure of the very thing the privilege is designed to protect." *Id.* at 8; *see id.* at nn.20-22.

In addition to citing the *Duncan* decision, *Reynolds* cited a handful of U.S. decisions that, according to *Reynolds*, demonstrate that the state-secrets privilege "is well established in the law of evidence." *Reynolds*, 345 U.S. at 6-7. Nowhere did the Court state that the privilege has a constitutional provenance.[4] *Reynolds*

[4] *Reynolds* characterized as having "constitutional overtones" the government's argument that "executive department heads have power to withhold any documents in their custody from judicial view if they deem it to be in the public interest," as to which the government claimed "an inherent executive power

(Continued on following page)

is expressly rooted exclusively in the common-law construct of an evidentiary privilege.

The operation of the state-secrets privilege in *Reynolds* demonstrates its nature as a common-law evidentiary rule. As with any other common-law privilege, whether the state-secrets privilege applies is a matter for judicial, not executive, determination. "Judicial control over the evidence in a case cannot be abdicated to the caprice of executive officers." *Reynolds*, 345 U.S. at 9-10. In the application of the attorney-client privilege or any other common-law evidentiary privilege, the effect of the privilege is to exclude the privileged evidence. The same is true of the common-law state-secrets privilege: "The effect of the government's successful invocation of privilege 'is simply that the evidence is unavailable, as though a witness had died, and the case will proceed accordingly, with no consequences save those resulting from the loss of evidence.'" *Al-Haramain Islamic Foundation, Inc. v. Bush*, 507 F.3d 1190, 1204 (9th Cir. 2007) (quoting *Ellsberg v. Mitchell*, 709 F.2d 51, 64 (D.C. Cir. 1983)); *accord, In re Sealed Case*, 494 F.3d 139, 144-45, 149-51 (D.C. Cir. 2007). That is what happened in *Reynolds*, where this Court said that,

which is protected in the constitutional system of separation of power," as well as the respondents' argument that "the executive's power to withhold documents was waived by the Tort Claims Act." *Reynolds*, 345 U.S. at 6 & n.9. However, the Court found it "unnecessary to pass upon" those arguments, "there being a narrower ground for decision." *Id.* at 6.

notwithstanding the government's successful invocation of the state-secrets privilege, "it should be possible for respondents to adduce the essential facts as to causation without resort to material touching upon military secrets." *Reynolds*, 345 U.S. at 11.[5]

[5] The state-secrets evidentiary privilege, which results only in the exclusion of evidence, is to be distinguished from the rule that a lawsuit is nonjusticiable if its "very subject matter" is an attempt to enforce duties arising out of a voluntary secret relationship between the plaintiff and the government. *See Tenet v. Doe*, 544 U.S. 1, 8 (2005); *Totten v. United States*, 92 U.S. 105, 107 (1875). In *Tenet*, this Court made clear that the nonjudiciability rule applies *only* to lawsuits seeking to enforce such duties *See Tenet*, 544 U.S. at 3 ("the longstanding rule, announced more than a century ago in *Totten*, prohibit[s] suits against the Government based on covert espionage agreements"); *id.* at 8 ("*Totten* precludes judicial review in cases such as respondents' where success depends upon the existence of their secret espionage relationship with the Government"); *id.* at 9 ("*Totten's* broader holding [is] that lawsuits premised on alleged espionage agreements are altogether forbidden"). *Tenet* carefully distinguished the state-secrets privilege of *Reynolds* from the nonjudiciability rule for suits enforcing espionage agreements: "We recognized [in *Reynolds*] 'the privilege against revealing military secrets, a privilege which is well established in the law of evidence,' and we set out a balancing approach for courts to apply in resolving Government claims of privilege." (*Id.* at 9 (citations omitted) (quoting *Reynolds*, 345 U.S. at 6-7) "[T]he categorical *Totten* bar," by contrast, applies "in the distinct class of cases that depend upon clandestine spy relationships." *Id.* at 9-10. In the present case, the Court of Appeals thus erred when in a dictum it conflated the *Totten/Tenet* bar with the state-secrets privilege. *See McDonnell Douglas Corp. v. United States*, 323 F.3d at 1021. That error, however, in addition to being a dictum, is not within the scope of this Court's grant of certiorari.

B. The Majority View Among the Lower Federal Courts is that the State-Secrets Privilege is a Judge-Made Evidentiary Rule Without Foundation in the Constitution.

Not surprisingly, given how *Reynolds* characterized the provenance of the state-secrets privilege, nearly all of the post-*Reynolds* decisions on point have described the state-secrets privilege as a common-law evidentiary rule. *See, e.g., Mohamed v. Jeppesen Dataplan, Inc.*, 614 F.3d 1070, 1077 (9th Cir. 2010) (the state-secrets privilege as applied in *Reynolds* "is an evidentiary privilege"); *Doe v. Central Intelligence Agency*, 576 F.3d 95, 101 (2d Cir. 2009) ("the Supreme Court [in *Reynolds*] established the procedure by which federal courts police the government's invocation of the common-law state-secrets privilege"); *Al-Haramain*, 507 F.3d at 1196 ("The state secrets privilege is a common law evidentiary privilege"); *In re Sealed Case*, 494 F.3d at 142 ("The state secrets privilege 'is a common law evidentiary rule' "); *Monarch Assur. P.L.C. v. U.S.*, 244 F.3d 1356, 1358 (Fed. Cir. 2001) (CIA Director's affidavit "invoked the common-law state secrets privilege"); *Kasza v. Browner*, 133 F.3d 1159, 1167 (9th Cir. 1998) ("the state secrets privilege is an evidentiary privilege rooted in federal common law"); *Zuckerbraun v. General Dynamics Corp.*, 935 F.2d 544, 546 (2d Cir. 1991) ("The state secrets privilege is a common law evidentiary rule"); *In re United States*, 872 F.2d 472,

474 (D.C. Cir. 1989) ("The state secrets privilege is a common law evidentiary rule").

In *Jeppesen Dataplan*, where the Ninth Circuit upheld an assertion of the state-secrets privilege, a six-judge majority of an eleven-judge en banc panel stated that the privilege is "a judge-made doctrine." 614 F.3d at 1092. That statement appeared in the following context:

> *For all the reasons the dissent articulates* – including the impact on human rights, the importance of constitutional protections *and the constraints of a judge-made doctrine* – we do not reach our decision lightly or without close and skeptical scrutiny of the record and the government's case for secrecy and dismissal.

Id. (emphasis added). The dissent described the state-secrets privilege as "a judicial construct *without foundation in the Constitution*." *Id.* at 1094 (Hawkins, J., dissenting) (emphasis added). Thus, the majority endorsed the dissent's articulation of the state-secrets privilege as *lacking a constitutional basis*. All eleven members of the en banc panel agreed with that articulation.

Congress has likewise viewed the state-secrets privilege as lacking a constitutional basis. In 1972, when this Court transmitted its proposed Federal Rules of Evidence to Congress, the proposal included a rule defining the "secrets of state" privilege. Congress intervened and redrafted the Federal Rules of

Evidence, and in the course of doing so both the House and the Senate described the state-secrets privilege as one of numerous "nonconstitutional" privileges. H.R. Rep. No. 93-650 (1973), *reprinted in* 1974 U.S.C.C.A.N. 7075, 7082; S. Rep. 93-1277 (1974), *reprinted in* 1974 U.S.C.C.A.N. 7051, 7058. (Ultimately, Congress "eliminate[d] all of the Court's specific Rules on privileges" in favor of "a single Rule 501," which "left the law of privileges in its present state." H.R. Rep. No. 93-650, *reprinted in* 1974 U.S.C.C.A.N. at 7082.)[6]

[6] Congress has regulated the state-secrets privilege's invocation in criminal cases via the Classified Information Procedures Act (CIPA), 18 U.S.C. App. 3 For example, section 6 of CIPA authorizes courts "to conduct a hearing to make all determinations concerning the use, relevance, or admissibility of classified information," *id.* § 6(a), and, upon "any determination by the court authorizing the disclosure of specific classified information under the procedures established by this section," authorizes courts to order "the substitution for such classified information of a statement admitting the relevant facts that the specific classified information would tend to prove" or "the substitution for such classified information of a summary of the specific classified information," *id.* § 6(c).

Similarly, in FISA, Congress has displaced the state-secrets privilege with a comprehensive statutory scheme regulating the use of secret evidence in litigation involving electronic surveillance. 50 U.S.C. § 1806(f); *National Security Agency Telecommunications Records Litigation*, 564 F. Supp 2d at 1124 ("[T]he parties' disagreement over the origins of the state secrets privilege is of little practical significance. Whether a 'clear statement,' a comprehensive legislative scheme or something less embracing is required, Congress has provided what is necessary for this court to determine that FISA preempts or

(Continued on following page)

C. The Confluence of the State-Secrets Privilege and Article II Duties Does Not Give the Privilege a Constitutional Provenance.

A minority view among the lower federal courts ascribes constitutional significance to the state-secrets privilege. In *El-Masri v. United States*, 479 F.3d 296 (2d Cir. 2007), the court observed: "Although the state secrets privilege was developed at common law, it performs a function of constitutional significance, because it allows the executive branch to protect information whose secrecy is necessary to its military and foreign-affairs responsibilities." *Id.* at 303; *accord, Arar v. Ashcroft*, 585 F.3d 559, 581 n.14 (2d Cir. 2009) (quoting *El-Masri*); *see also* Chesney, *supra*, 75 GEO. WASH. L. REV. at 1270, 1309-10 (describing some early pronouncements of the state-secrets privilege as having "constitutional overtones" and suggesting "[i]t might be best, then, to conceive of the state secrets privilege as having a potentially inalterable constitutional core surrounded by a revisable common-law shell"); Brief of Petitioner The Boeing Company at 31 n.10 (citing *El-Masri*).

The court in *El-Masri* relied on *United States v. Nixon*, 418 U.S. 683, 710 (1974), quoting a dictum in *Nixon* which characterized the protection of "'military

displaces the state secrets privilege. . ."); *see also Jeppesen Dataplan*, 614 F.3d at 1092 n.15 ("Congress presumably possesses the power to restrict application of the state secrets privilege").

or diplomatic secrets'" as being within "'areas of Art. II duties [where] the courts have traditionally shown the utmost deference to Presidential responsibilities.'" *El-Masri*, 479 F.3d at 303 (quoting *Nixon*, 418 U.S. at 710). According to *El-Masri*, the Court in *Nixon* "articulated the [state secrets] doctrine's constitutional dimension." *Id.* But *El-Masri* wrongly imbued the state-secrets privilege with a constitutional provenance, by misconstruing the *Nixon* dictum.

Nixon adjudicated an invocation of *executive* privilege, deciding nothing with regard to the state-secrets privilege. The Court explained:

> In this case the President challenges a subpoena served on him as a third party requiring the production of materials for use in a criminal prosecution; he does so on the claim that he has a privilege against disclosure of confidential communications. He does not place his claim of privilege on the ground they are military or diplomatic secrets.

Nixon, 418 U.S. at 710. This explanation is followed by the dictum that "[a]s to these areas of Art. II duties the courts have traditionally shown the utmost deference to Presidential responsibilities." *Id.* The dictum places the President's protection of "military or diplomatic secrets" within the "areas of Art. II duties." *Id.*

This dictum merely describes a confluence of the state-secrets privilege and Article II duties in the context of civil litigation, where the privilege, like any

other rule of federal common law, is a means at the President's disposal in the exercise of executive power. The state-secrets privilege is of no more constitutional provenance than any other rule of federal common law: The Judiciary implements those common-law rules as a necessary adjunct of its Article III power to adjudicate cases and controversies, even though the content of those common-law rules is not compelled or determined by the Constitution. Thus, the Executive is free to assert the state-secrets privilege, just as the Executive is free to assert any other privilege or rule of procedure in furtherance of Article II duties, but it is up to the courts to define the privilege and control its application.

The district court in the *Al-Haramain* case made this point when discussing the defendants' argument that the state-secrets privilege has a constitutional basis in Article II. *National Security Agency Telecommunications Records Litigation,* 564 F. Supp. 2d at 1122-24. The court began its discussion as follows:

> *Reynolds* itself, holding that the state secrets privilege is part of the federal common law, leaves little room for defendants' argument that the state secrets privilege is actually rooted in the Constitution. *Reynolds* stated that the state secrets privilege was "well-established in the law of evidence." 345 U.S. at 607, 73 S.Ct. 528. At the time, Congress had not yet approved the Federal Rules of Evidence, and therefore the only "law of evidence" to apply in federal court was an

> amalgam of common law, local practice and statutory provisions with indefinite contours.

Id. at 1123.

Next, the court observed that "all rules of federal common law have some grounding in the Constitution," in that "'[f]ederal common law implements the federal Constitution and statutes, and is conditioned by them.'" *Id.* (quoting *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 472 (1942) (Jackson, J., concurring)). "Accordingly, all rules of federal common law perform a function of constitutional significance." *Id.*

The court concluded, however, that this feature of the federal common law does not imbue it with a constitutional provenance:

> In the specific context of the state secrets privilege, it would be unremarkable for the privilege to have a constitutional "core" or constitutional "overtones." [Citing Chesney, 75 GEO. WASH. L. REV. at 1309-10.] Article II might be nothing more than the source of federal policy that courts look to when applying the common law state secrets privilege. *But constitutionally-inspired deference to the executive branch is not the same as constitutional law.*

Id. (emphasis added).

In other words, executive protection of state secrets is an Article II power, but invocation of the state-secrets privilege as a means for protecting national security is not the invocation of a constitutionally-compelled rule.

Rather, the state-secrets privilege is a common-law evidentiary rule inspired by policy considerations that predate the Constitution; it is not imposed on the courts by Article II, even though the Executive may invoke it in the course of performing the Executive's Article II responsibilities. Likewise, judicial deference to the Executive's invocation of the state-secrets privilege is constitutionally inspired, but the substance of the privilege is not of constitutional provenance. That is all this Court meant in *Nixon* when observing that the protection of state secrets is within "areas of Art. II duties" to which "the courts have shown the utmost deference." *Nixon*, 418 U.S. at 710.

The state-secrets privilege is not mentioned anywhere in Article II. Indeed, the Constitution has nothing to say about secrecy of any sort, other than to give Congress the power to keep its proceedings secret. *See* U.S. CONST., art. I, § 5, cl. 3. The provenance of the state-secrets privilege lies in the common law, not the Constitution.

•

CONCLUSION

Should the Court address the provenance of the state-secrets privilege, the Court should conclude that the state-secrets privilege is a common-law evidentiary rule of nonconstitutional provenance.

Respectfully submitted,

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AMICUS CURIAE BRIEF

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Nos. 09-1298, 09-1302

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GENERAL DYNAMICS CORPORATION,
Petitioner,

v.

UNITED STATES,
Respondent.

THE BOEING COMPANY, SUCCESSOR TO
MCDONNELL DOUGLAS CORPORATION,
Petitioner,

v.

UNITED STATES,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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INTEREST OF THE *AMICUS CURIAE*

The Chamber of Commerce of the United States of America (the Chamber) submits this brief as *amicus curiae* in support of petitioners General Dynamics Corporation and The Boeing Company.[1]

The Chamber is the world's largest business federation. The Chamber represents more than 300,000 direct members and indirectly represents an underlying membership of more than three million companies and professional organizations of every size, in every industry sector, and from every region of the country. An important function of the Chamber is to represent the interests of its members in matters before Congress, the Executive Branch, and the courts. To that end, the Chamber regularly files *amicus* briefs in cases that raise issues of vital concern to the nation's business community. This is such a case.

Many members of the Chamber do business with the federal government. The Chamber also represents businesses in industries, such as defense and aerospace, transportation, information technology, and telecommunications, which long have served the nation by entering contracts to provide the federal government with goods and services that are vital to the nation's security. Such contracts often relate to defense or national security programs that are highly classified. For this reason, the question

[1] Pursuant to Supreme Court Rule 37.6, *amicus curiae* states that no counsel for any party authored this brief in whole or in part and that no entity or person, aside from *amicus curiae*, its members, and its counsel, made any monetary contribution towards the preparation and submission of this brief. Counsel of record for all parties have consented to the filing of this brief in letters on file with the Clerk's office.

presented in this case—whether the Government may prevail in its contract claim against a contractor because its assertion of the state secrets privilege completely deprives the contractor of its facially valid defense to that claim—is of particular concern to the Chamber and its members.

INTRODUCTION AND SUMMARY OF ARGUMENT

This case concerns whether the federal government may protect classified information by invoking the state secrets privilege *and* allow that privilege to serve as the basis for the Government to prevail on its own contract claim against defense contractors. While honoring the invocation of the privilege is quite proper, allowing the federal government to gain financially from the privilege at the expense of the Government's contractor is unconscionable. Sustaining a government claim worth billions of dollars after the Government's invocation of the privilege has eliminated the contractor's defense does serious violence to basic due process principles that have uniformly and appropriately guided judicial resolution of how the state secrets doctrine affects pending claims. In addition, significant commercial uncertainty would arise in the defense procurement process if the Government were permitted not only to define private parties' contract rights by establishing the government contracting system and negotiating individual defense contracts, but also to nullify certain of those rights on an ad hoc basis as particular contract disputes arise.

In this case, the Federal Circuit held that the invocation of the state secrets privilege protected the Government's classified information and permitted the Government to prevail in its multi-billion-dollar

claim against two government contractors selected by the Navy to design and build an aircraft using highly classified stealth technology. Under the Federal Circuit's approach, invoking the privilege eliminated the contractors' key defense against the Government's claim that the contractors' delay placed them in contractual default. That defense was that the Government failed to share its "superior knowledge" and critical information that was necessary to prevent them from pursuing a "ruinous course of action."[2] App. 202a. Because the contractors were stripped of their ability to argue on this basis that the Government's actions should be deemed a termination of the contract for convenience, rather than based on the contractors' default, the Federal Circuit ruled in favor of the Government on its default termination claim. As a result, the Government is demanding that the contractors return approximately $2.9 billion in progress payments and interest (see General Dynamics Br. at 21), and the contractors will not be reimbursed for the $1.2 billion in unreimbursed costs (now more with interest) the Court of Federal Claims found they spent performing the contract before it was terminated by the Government (see Boeing Br. at 17).

The court of appeals' decision causes great uncertainty for businesses that enter contracts with the Government that relate to classified matters affecting national security, homeland security, and intelligence matters. Under the Federal Circuit's rule, these businesses have little assurance that their contractual rights and defenses will be judicially enforced where the Government may assert that

[2] Citations to the Petition Appendix are to the Appendix to the Petition for Writ of Certiorari filed by General Dynamics in No 09-1298.

relevant evidence is protected by the state secrets privilege. Contractors have little basis to assess or contract around the risk of the Government invoking the privilege. The court's decision "expand[s] the Government's opportunities for contractual abrogation, with the certain result of undermining the Government's credibility at the bargaining table and increasing the cost of its engagements," *United States* v. *Winstar Corp.*, 518 U.S. 839, 884 (1996) (plurality opinion), the very result this Court has sought to avoid in cases where the Government has breached its contractual obligations and attempted to walk away cost-free. If the Federal Circuit's decision stands, the defense contracting process would shift from one grounded in rule of law principles toward a less workable, one-sided deal that gives the United States so much leverage that contractors may be unwilling to enter into such arrangements. Cf. *id.* at 913 (Breyer, J., concurring) (where Government can breach contract with impunity, private businesses might "quite rightly, be unwilling to undertake the risk of government contracting").

This Court can restore certainty to the contracting process without calling into question the Government's legitimate ability to invoke the state secrets privilege and shield classified information from disclosure in this or any other case. In the Chamber's view, the Government is fully empowered to protect sensitive information, such as the stealth aircraft technology at issue in this case. Here, the state secrets privilege was properly invoked because a sufficiently senior official determined that disclosure reasonably could be expected to "'severely

jeopardize national security.'"[3] App. 375a (quoting declaration of Secretary Donley). The proper invocation of the privilege should not, however, allow a court to enter judgment for the Government on its default termination claim if the privilege prevents the contractors from defending against the Government's assertion that they were in default. The Government's claim instead should be resolved by applying the most basic principles of fundamental fairness and due process, with the effect of accommodating the nation's security interests and restoring contractual certainty. Lower courts correctly dismiss claims brought against the Government, government contractors, or others when the Government's invocation of the state secrets privilege deprives the plaintiff of evidence needed to establish *prima facie* case—or deprives the defendant of evidence needed to present a defense. Dismissal of claims in the latter case is a logical and proper implication of basic due process principles: courts cannot order relief against a party that is precluded from defending itself. *Nelson* v. *Adams USA, Inc.*, 529 U.S. 460, 466 (2000). This Court should apply those principles here.

These principles should especially support dismissal of the Government's claim against a defense contractor. The Government, acting in its sovereign capacity, has already protected its interests by enacting the Contract Disputes Act and promulgating the Federal Acquisition Regulation, which establishes the contract dispute process and gives the Government unique rights, such as the right to terminate a contract for its own convenience.

[3] The Chamber's knowledge of the facts of this case is limited to those set forth in the lower court opinions reprinted in the Petition Appendices.

The Government, acting in its propriety capacity, further protects its interests by negotiating the terms of particular contracts. The Government, acting as a litigant advancing a contract claim in federal court, should not be permitted in addition to use its authority to protect state secrets to eliminate a contractor's *prima facie* defense, thereby securing to the United States an enormous financial windfall and imposing on the contractor an equally enormous out-of-pocket loss. Due process precludes that outcome, where the Government blatantly attempts to shift "the costs of meeting its legitimate public responsibilities to private parties." *Winstar*, 518 U.S. at 896.

ARGUMENT

I. ELIMINATING DEFENSES AGAINST A GOVERNMENT CLAIM BASED ON THE STATE SECRETS DOCTRINE WOULD CREATE COMMERCIAL UNCERTAINTY, IMPAIRING THE PROVISION OF GOODS AND SERVICES NEEDED FOR THE NATIONAL DEFENSE.

The Federal Circuit held that the Government's invocation of the state secrets privilege eliminates a contractors' "superior knowledge" defense in a government contract dispute and that as a result the Government prevails in its contract claim. The court rejected the traditional approach that protects classified information and bars the prosecution of any claim where the invocation deprives a party of a defense to the claim. By enabling the invocation of the privilege to defeat a contractual right held against the Government, the Federal Circuit's rule creates considerable uncertainty surrounding the enforceability of government contracts that directly

or indirectly involve classified matters. That result, in turn, threatens to undermine and make less efficient the government contract system the United States has long used to procure the goods and services that are critical to the nation's security—with the inevitable result that costs will increase or fewer services will be provided. In sum, allowing the state secrets doctrine to be used as it has in this case is both bad government contracting practice and hopelessly inconsistent with any notion of due process.

A. The United States Has Always Relied On Contractors To Provide Goods And Services For The National Defense, Including Those Needed For Classified Programs.

The United States has always relied on the innovation and efficiency of the private sector to provide goods and services for the national defense. This practice is quite unlike that of most former and current Communist nations, which rely instead on instrumentalities of the government, or many European nations, which rely on companies substantially owned by the government. In 1775, the Continental Congress established a procurement system and appointed a quartermaster general and a commissary general to procure clothing, weapons, transportation and engineering services for the Continental Army.[4] As the threats facing the nation and the needs of the military changed over the next two centuries, the Government continued its reliance

[4] *See* Moshe Schwartz, Congressional Research Service, *Defense Acquisitions: How DOD Acquires Weapon Systems and Recent Efforts to Reform the Process* 1-2 (July 10, 2009), *available at* http://www.fas.org/sgp/crs/natsec/rl34026.pdf.

on private enterprise. During World War II, for example, "Congress sought to do everything possible to retain and encourage individual initiative in the world-wide race for the largest and quickest production of the best equipment and supplies." *Lichter* v. *United States*, 334 U.S. 742, 768 (1948).

The private sector continues to be vital to homeland security and national defense today because "the vast majority of critical [defense industrial base] assets reside in the private sector."[5] Thousands of suppliers now contract with the Department of Defense to provide the weapons, equipment, and raw materials to achieve national security objectives.[6] In 2009, the Department of Defense purchased more than $380 billion in goods and services from the nation's top 100 defense contractors.[7] And in fiscal year 2010, outlays on national defense were estimated to represent almost 20 percent of total federal outlays and almost five percent of gross domestic product.[8]

[5] U.S. Dep't of Homeland Security, *National Infrastructure Protection Plan, Defense Industrial Base Sector* 2, *available at* http://www.dhs.gov/xlibrary/assets/nipp_snapshot_defenseindustrialbase.pdf.

[6] Gov't Accountability Office, *DOD Assessments of Supplier-Base Availability for Future Defense Needs; Briefing to the Senate Committee on Banking and Housing, Urban Affairs, Subcommittee on Security and International Trade and Finance* 2 (Oct. 27, 2009), *available at* http://www.gao.gov/new.items/d10317r.pdf.

[7] Gov't Executive, *Top 100 Defense Contractors* (Aug. 15, 2010), *available at* http://www.govexec.com/story_page_pf.cfm?articleid=43388&printerfriendlyvers=1.

[8] U.S. Dep't of Commerce, *Statistical Abstract of the United States: 2010*, tbl.491, at 326, *available at* http://www.census.gov/prod/2009pubs/10statab/defense.pdf.

As this case and earlier cases illustrate, the application of the state secrets privilege often arises in the context of—and has the potential to affect—the development and manufacture of the most advanced, and thus most classified, technologies used by the military. *United States* v. *Reynolds*, 345 U.S. 1 (1953) (testing of secret electronic equipment aboard a B-29 aircraft); *Crater Corp.* v. *Lucent Techs., Inc.*, 423 F.3d 1260 (Fed. Cir. 2005) (development and manufacture of underwater coupling device for fiber optics); *Bareford* v. *Gen. Dynamics, Corp.*, 973 F.3d 1138 (5th Cir. 1992) (design and manufacture of Navy's Phalanx anti-missile system); *Bentzlin* v. *Hughes Aircraft Co.*, 833 F. Supp. 1486 (C.D. Cal. 1993) (manufacture of air-to-ground missile used by the Air Force during Operation Desert Storm); *Nejad* v. *United States*, 724 F. Supp. 753 (C.D. Cal. 1989) (design and manufacture of Navy's AEGIS ship-based air defense system). Cases concerning the state secrets doctrine have also addressed support allegedly provided by companies to intelligence agencies. *E.g. Mohamed* v. *Jeppesen Dataplan, Inc.*, 614 F.3d 1070 (9th Cir., 2010) (en banc) (alleged provision of counter-terrorism-related transport service to intelligence agency); *Hepting* v. *AT&T Corp.*, 439 F. Supp. 2d 974 (N.D. Cal. 2006) (alleged telecommunications support to National Security Agency). Thus, the defense and intelligence communities and the nation in general have been well served by government contractors.

B. The Federal Circuit's Rule Would Undermine the Contractual Certainty That Underpins The Defense Sector's Ability To Provide Goods And Services To The Government.

As Justice Brandeis recognized, "[p]unctilious fulfillment of contractual obligations is essential" to the government's ability to enter contracts. *Lynch* v. *United States*, 292 U.S. 571, 580 (1935). Since the Government first waived sovereign immunity for contract claims in 1855, the assurance that private companies can enforce their contracts with the Government has been viewed as "indispensable to the efficient operation of government, for without it, qualified private contractors might not undertake government projects ...." Harold J. Krent, *Reconceptualizing Sovereign Immunity*, 45 Vand. L. Rev. 1529, 1565 (1992).

Today, the Federal Acquisition Regulations govern the award, performance and termination of government contracts through rules intended to ensure that the private sector can "deliver on a timely basis the best value product or service to the [Government], while maintaining the public's trust and fulfilling public policy objectives." 48 C.F.R. § 1.102(a). If a government contractor believes the Government has not complied with its contractual obligations, it may file a claim with the contracting officer. 41 U.S.C. § 605(a). Likewise, if the Government believes that a contractor is in breach of its obligations, the contracting officer may find that the contractor is in default and terminate the contract. *Id.*; see also *Malone* v. *United States*, 849 F.2d 1441, 1443 (Fed. Cir. 1988). The contracting officer's decision "shall be final and conclusive and not subject to review by any forum, tribunal, or

Government agency, unless an appeal or suit is timely commenced," 41 U.S.C. § 605(b), by the contractor filing an appeal to the agency board of contract appeals, *id.* § 606, or a lawsuit in the Court of Federal Claims, *id.* § 609(a).

One effect of the contracting officer's decision to terminate the contract for default is that the Government is "not liable for the contractor's costs on undelivered work and is entitled to the repayment of advance and progress payments, if any, applicable to that work." 48 C.F.R. § 49.402-2(a). A default termination can also harm the contractor's ability to obtain future government contracts, or even result in the contractor's debarment from future government contracts. See *Malone*, 849 F.2d at 1445; *Bannum, Inc.* v. *United States*, 91 Fed. Cl. 160, 171-72 (2009).

This scheme has two remarkable qualities. First, a termination for default obviously carries with it extraordinarily negative consequences for the government contractor. It not only deprives the contractor of the potential profit in the contract, but also requires disgorgement of monies received for services actually rendered on the Government's behalf and threatens the contractor's ability to receive future government contracts. Thus, the termination for default can be described as the "death penalty" in government contracting.

Second, even though a claim that the contractor is in default of a contract is a *Government* claim for which the Government bears the burden of proof, *Malone*, 849 F.2d at 1443, the statutory scheme does not require the Government to bring suit to establish the contractor's liability. See also Pet. Opp. at 14-15 (conceding that "default termination has been deemed a 'government claim' . . . for which the government bears the burden of proof under the

CDA"). Instead, the statutory scheme provides that the contracting officer's default termination decision is final and unreviewable in any forum unless it is challenged by the *contractor* in the Court of Federal Claims or the relevant agency board of contract appeals. 41 U.S.C. § 605(b); *Seaboard Lumber Co.* v. *United States*, 903 F.2d 1560, 1562 (Fed. Cir. 1990).

The Government's claim in this case was initially adjudicated through just this process. The contracting officer granted the Government's claim that the contractors were in default and terminated the contract. App. 8a. A few weeks later, the Navy sent the contractors a letter demanding the return of approximately $1.35 billion in unliquidated progress payments under the contract. *Id.* Had the contractors not filed suit challenging the default termination, that determination would have become final and unreviewable. That determination did not become final, however, because the contractors filed suit, claiming that they were not in default because, among other reasons, the Government breached its duty to disclose its "superior knowledge" and the "critical information" necessary to prevent them from "unknowingly pursuing a ruinous course of action." App. 202a. Specifically, the Government had extensive knowledge concerning stealth technology that the contractors lacked. With that technology, it is alleged, the contractors would have fulfilled all of their contractual obligations in timely fashion. But without that technology, Boeing and General Dynamics were left to flounder in search of sophisticated solutions to extremely complicated technical problems. This is the classic situation where the party who fails to comply with the contract is found not to be in breach of contract. See, *e.g.*, *Fla. Engineered Constr. Prods. Corp.* v. *United* States, 41

Fed. Cl. 534, 542 (1998) (contractor may raise Government's failure to share superior knowledge as a complete defense to Government's default termination claim). After the Government invoked the state secrets privilege to preclude discovery of evidence necessary to litigate the contractors' superior knowledge defense, the trial court concluded that the defense "could not be tried because the resulting threat to national security would not permit it." App. 243a-244a.

At this point, however, the courts below abandoned the traditional approach to implementing the state secrets privilege and created the rule that so threatens contract rights and the commercial certainty that the government contracting process depends upon for success. Instead of dismissing the Government's default termination claim because the state secrets privilege deprived the contractors of the superior knowledge defense, see *infra* pp. 18-21 (outlining traditional approach), the Court of Federal Claims dismissed only the contractors' superior knowledge defense (App. 246a) and entered judgment for the Government on its default termination claim (App. 177a). That is, the court allowed the Government to prevail based on the Government's own actions that eliminated the contractors' defense.

In affirming this decision, the Federal Circuit granted the Government a wholly one-sided and purely discretionary means of avoiding its contractual commitments in cases involving sensitive classified information. The natural and inevitable result of this contractual uncertainty is to undermine the defense sector's ability and willingness to enter such contracts, which "produce[s] the untoward result of compromising the Government's practical capacity to make contracts[.]" *Winstar*, 518 U.S. at 884. And,

where contractors are willing to enter contracts despite the increased commercial uncertainty, they must address that increased risk as any other commercial party would—through increased charges or reduced service provision. But this Court has routinely rejected Government efforts to achieve short-term gains by trying to short-change contractors, recognizing that the long-term consequences to the public interest would be much worse if the Government were to prevail in a particular dispute on a theory that would broadly harm the contracting community. *Id.;* see also *id.* at 913 (Breyer, J., concurring) (rules promoting contractual certainty "ensure[] that the government is able to obtain needed goods and services from parties who might otherwise, quite rightly, be unwilling to undertake the risk of government contracting"); *id.* at 921 (Scalia, J., concurring) (contract should not be read to make the Government's performance discretionary). To be sure, the amount of money involved in this dispute is not insignificant, but it will pale in comparison to the ultimate costs the United States will incur in the event that all government contractors must turn a jaundiced eye to every agreement they are asked to enter into that implicates government secrets.

II. THE STATE SECRETS PRIVILEGE CAN AND SHOULD BE IMPLEMENTED TO PROTECT BOTH THE GOVERNMENT'S MILITARY AND INTELLIGENCE SECRETS AND THE CONTRACTUAL RIGHTS OF DEFENSE CONTRACTORS.

This case presents no occasion to balance the nation's security against the rights of litigants, or to reconsider the entirely appropriate rule that courts should defer to the determination by sufficiently

senior Executive Branch officials that sensitive national security information should be protected from disclosure in litigation. Instead, resolving this case requires only the application of established principles already developed in cases determining the litigation consequences of the Government's invocation of the state secrets privilege. Those principles require dismissal of a claim when information subject to the state secrets privilege is necessary to a private party's ability to litigate either the claim or especially a defense to a claim before the court. Any other result would be inconsistent with due process principles.[9] Here, those principles require dismissal of a claim whereby the Government seeks to have a court find the contractors liable on a contract claim on which it seeks payment of billions of dollars by parties who cannot defend themselves due solely to the Government's invocation of the privilege.

A. The State Secrets Privilege Should Reflect And Protect the Government's Authority To Control Access To Classified Information.

This case appropriately focuses on the litigation consequences of the Government's invocation of the state secrets privilege, rather than on the conditions or processes that may give rise to the assertion of the privilege. Defense contractors often handle the most sensitive national security information on the Government's behalf and appreciate that only senior government officials have the full scope of

[9] The Court could resolve this case based on the Due Process Clause or avoid the constitutional issue by implementing the privilege to require the dismissal of the Government's default termination claim.

information and expertise needed to assess the potential harm that release of information may pose to the nation's security. Courts appropriately defer to the Government's invocation of the privilege, and accordingly protect sensitive national security information. See *infra* pp. 16-18. In contrast, courts cannot defer to the Government's preferences regarding the judicial actions required once that information is protected from disclosure.

For reasons "too obvious to call for enlarged discussion," *CIA* v. *Sims*, 471 U.S. 159, 170 (1985), the "protection of classified information must be committed to the broad discretion of the agency responsible, and this must include broad discretion to determine who may have access to it." *Dep't of Navy* v. *Egan*, 484 U.S. 518, 529 (1988). Businesses that enter contracts with the Government therefore understand that the relevant federal agency decides whether information relating to the contract should be classified. See Exec. Order 13526, 75 Fed. Reg. 707 (Dec. 29, 2009). If classified information is released to a government contractor, the contractor also understands that the information must "be safeguarded in a manner equivalent to its protection within the executive branch of Government." Exec. Order 12829, 58 Fed. Reg. 3479 (Jan. 6, 1993).

Government contracts involving classified information contain a "Security Requirements" clause restricting the disclosure of classified information, 42 C.F.R. § 4.404, and employees of government contractors must certify that they will abide by the restrictions on the release of classified information. See Information Security Oversight Office, *Classified Information Nondisclosure Agreement Briefing Booklet, available at* http://www.archives.gov/isoo/training/standard-form-312.html. Sanctions associat-

ed with contractors' disclosure of classified information are severe. The Government "may move to terminate the contract or to seek monetary damages from the contractor, based on the terms of the contract" and may also criminally prosecute individuals or organizations. *Id.* at Question 20.

The Government also appropriately controls disclosure of, and access to, classified information in litigation. The common law has long recognized a privilege for the government to withhold information in the interest of national security. See *Reynolds*, 345 U.S. at 7 (discussing English cases); *United States* v. *Burr*, 25 F. Cas. 30, 37 (C.C.D. Va. 1807) (No. 14692D) (Marshall, C.J.) (suggesting that a letter from a general might be privileged if it "contains any matter the disclosure of which would endanger the public safety").

In *Reynolds,* this Court established an appropriate framework for the Government's invocation of the state secrets privilege. To ensure that a suitably knowledgeable and accountable Executive Branch official makes the national security assessment, the privilege must be asserted by the "head of the department which has control over the matter, after actual personal consideration by that officer." *Reynolds,* 345 U.S. at 8. To ensure that the Executive Branch articulates the basis for its conclusions and sets forth the degree of potential harm to the nation's security, the "court itself must determine whether the circumstances are appropriate for the claim of privilege, and yet do so without forcing a disclosure of the very thing the privilege is designed to protect." *Id.* If the court is satisfied, "from all the circumstances of the case, that there is a reasonable danger that compulsion of the evidence will expose military matters which, in the interest of

national security should not be divulged," the Government may not be compelled to produce the evidence. *Id.* at 10-11.

The *Reynolds* framework is an entirely reasonable means to protect the national security while fostering the accountability of the Executive Branch, and it functioned in just that manner in this case. The contracting parties most familiar with information related to that withheld at the Government's request do not challenge the propriety of the Government's decision to invoke the state secrets privilege. Nor could a court or private party reasonably suggest that the general subject matter of the privileged material—details of the stealth technology protecting the Nation's most advanced aircraft—does not deserve protection from public disclosure Cf. *id.* at 10. The litigants do not call for greater judicial scrutiny of the Government's determination, or fault the lower courts' treatment of the invocation of the privilege or the related information itself. Instead, they rightly focus on whether their defense can be nullified, and the Government awarded a financial windfall, as a result of the Court's honoring the Executive Branch's assessment of the national security consequences of disclosing the privileged information.

B. A Claim Raised In Litigation Must Be Dismissed If The State Secrets Privilege Precludes Litigation Of Either The Plaintiff's Claim Or The Defendant's Defense.

This Court and lower courts have, in fact, already set forth the principles that govern the litigation consequences that follow once a court declines to permit or order release of information subject to a properly supported invocation of the state secrets

privilege. In broad terms, those principles focus on whether a party's claim can be fully litigated (and judicial relief thereafter ordered) in the absence of the information subject to the privilege. Claims that have no evidentiary support in the absence of the withheld information are dismissed, and claims subject to defenses that cannot be asserted in the absence of the withheld information are dismissed as well. See *infra* pp. 19-21. Those simple principles reflect a proper understanding of the role of the courts, which especially cannot order relief against a party that has been stripped of the ability to defend itself in court. Due process principles require no less and should require dismissal of the Government's claim in this case.

As this Court recognized in *Reynolds*, 345 U.S. at 11, in many cases it will be possible for the plaintiff to establish a *prima facie* case without the information protected by the state secrets privilege. In some cases, however, withholding the privileged information will deprive the plaintiff of the evidence needed to establish a case. *E.g.*, *El-Masri* v. *United States*, 479 F.3d 296, 309 (4th Cir. 2007) (dismissing plaintiff's lawsuit against CIA officials because "El-Masri would need to rely on witnesses whose identities, and evidence the very existence of which, must remain confidential in the interest of national security"); *Bareford*, 973 F.2d at 1142 (dismissing plaintiffs' tort suit against the manufacturer of the Phalanx anti-missile system because their "claim of manufacturing and design defects requires proof of what the Phalanx system was intended to do and the ways in which it fails to accomplish these goals," all information subject to the state secrets privilege). In that situation, the claim must be dismissed because there is simply no way to establish a right to recovery

without disclosing information that must, in the interest of national security, remain secret. Dismissal of a claim is unquestionably a "harsh sanction. But the results are harsh in either direction and the state secrets doctrine finds the greater public good – ultimately the less harsh remedy – to be dismissal." *Id.* at 1144; see also, *e.g.*, *Fitzgerald* v. *Penthouse Int'l, Ltd.*, 776 F.2d 1236, 1238 n.3 (4th Cir. 1985) ("When the state secrets privilege is validly asserted, the result is unfairness to individual litigants—through the loss of important evidence or dismissal of a case—in order to protect a greater public value").

In other cases more directly relevant to this case, the plaintiff may be able to establish a *prima facie* case without information protected by the state secrets privilege, but the defendant—usually the Government or a contractor that acted pursuant to a contract in a classified program—needs privileged information to establish a defense to the claim. In this situation, dismissal is even more clearly the appropriate remedy, although the justification is slightly different. *E.g.*, *Tenenbaum* v. *Simonini*, 372 F.3d 776 (6th Cir. 2004); *Kasza* v. *Browner*, 133 F.3d 1159 (9th Cir. 1998); *Molerio* v. *FBI*, 749 F.2d 815 (D.C. Cir. 1984) (Scalia, J.). "The fundamental requisite of due process of law is the opportunity to be heard." *Mullane* v. *Cent. Hanover Bank & Trust, Co.* 339 U.S. 306, 314 (1950) (internal quotation marks omitted). In the context of civil litigation, this principle means that courts must provide the defendant with "an adequate opportunity to defend against the imposition of liability." *Nelson*, 529 at 466. If the invocation of the state secrets privilege has the practical effect of depriving the defendant of the ability to raise a defense, the courts cannot,

consistent with the due process that they are charged to provide, allow the plaintiff to continue to litigate the claim. Indeed, it would be a "mockery of justice" for the court to impose liability erroneously because the evidence needed to establish the defense to the claim is protected by the state secrets privilege. *Molerio*, 749 F.2d at 825. This result is also entirely consistent with this Court's unanimous approach to barring litigation of matters in the intelligence context that inherently involve classified information. See *Tenet* v. *Doe*, 544 U.S. 1 (2005).

The Government has acknowledged the validity of these rules on many occasions and has invoked them to have courts dismiss claims brought by third parties against the United States or its contractors when the court cannot determine the defendant's liability without information protected by the state secrets privilege. See, *e.g.*, *Mohammed*, 614 F.3d at 1087 (agreeing with Government that plaintiffs' claims against a government contractor should be dismissed because "there is no feasible way to litigate Jeppesen's alleged liability without creating an unjustifiable risk of divulging state secrets"); *El-Masri*, 479 F.3d at 310 (dismissing plaintiffs' claims against the United States because ""virtually any conceivable response to [plaintiffs'] allegations would disclose privileged information"); *Zuckerbraun* v. *Gen. Dynamics Corp.*, 935 F.2d 544, 547 (2d Cir. 1991) (dismissing plaintiffs' claims against defense contractors where the "factual questions concerning the liability of the defendants" cannot be resolved without information that "is in its entirety classified and subject to the claim of privilege"). In these cases, the Government appropriately uses the state secrets privilege as a shield to protect against the imposition of liability on a claim the Government or its

contractors cannot fully defend without disclosing classified information that, in the interest of national security, must remain secret.

C. The Government May Not Use the State Secrets Privilege As A Sword To Further Its Claims Against Defense Contractors.

The principles of fundamental fairness that determine the litigation consequences of the state secrets privilege, outlined above, directly require that the Government's termination of contracts for default should be converted into a termination for convenience when invocation of the privilege eliminates the contractors' ability to defend the assertion of "default." The Government is entitled to no special treatment in this respect. Indeed, the Government's ability to manage its litigation risks related to the government contracting process, its ability to control when the privilege is invoked, and the contractual obligations it owes to defense contractors all decidedly favor refusing to allow the United States to assert that the termination of the contracts was for default.

Like a private contracting party, the Government protects its interests by negotiating favorable contract terms. But unlike a private party, the Government also protects its interests by establishing the laws and regulations that govern the resolution of disputes that arise under government contracts. The Government has protected its interests in just this fashion by enacting rules that give it unique rights—such as the right to terminate a contract for its own convenience—that private companies do not share. This case is extraordinary because the Government seeks yet another way to advance its contractual interests: by asking the courts to allow the Government to use the state secrets privilege not

simply as a shield to protect military secrets, but also as a sword to prevail on the Government's own contract claim by precluding litigation of a private party's contractual defense to that claim. In granting that request, the Federal Circuit sanctioned an unprecedented application of the state secrets privilege that deprives the contractors of due process.

The Federal Circuit's decision is inconsistent with the courts' longstanding refusal to allow litigants to use a privilege as both a sword and a shield. See, *e.g.*, *United States* v. *Rylander*, 460 U.S. 752, 761 (1983) (Fifth Amendment privilege against self-incrimination); *Bittaker* v. *Woodford*, 331 F.3d 715 (9th Cir. 2003) (attorney-client privilege). Only this rule is consistent with the requirement that litigants in our judicial system be afforded "an adequate opportunity to defend against the imposition of liability." *Nelson*, 529 U.S. at 466. For this reason, courts do not permit a party to advance a claim while refusing to disclose information that could provide its adversary with a defense to that claim: a litigant "should not be required to defend against a party who refuses to reveal the very information which might absolve [him] of all liability." *Wehling* v. *CBS*, 608 F.2d 1084, 1088 (5th Cir. 1979).

This reasoning applies equally to governments and private litigants. As this Court has recognized, allowing a government to promote its "litigation interests" by freely asserting both a claim and immunity in the same case "could generate seriously unfair results." *Lapides* v. *Bd. Of Regents*, 535 U.S. 613, 619 (2002). Consequently, a state government may not advance its claim, or deflect counterclaims, by invoking state sovereign immunity, including that recognized by the Eleventh Amendment. *Id.* For example, when a state files a bankruptcy claim, "it

waives any immunity which it otherwise might have had respecting the adjudication of the claim." *Gardner* v. *New Jersey*, 329 U.S. 565, 574 (1947). Likewise, a foreign government may not pursue a claim and assert foreign sovereign immunity as a defense to that claim (or as to counterclaims). See 28 U.S.C. § 1607; *Cabiri* v. *Gov't of Ghana*, 165 F.3d 193 (2d Cir. 1999); see also 28 U.S.C. § 1605(a)(1). And, when the United States commences a civil action against a private party, the "defendant may, without statutory authority," assert a counterclaim to recoup "an amount equal to [the Government's] principal claim." *United States* v. *U.S. Fid. & Guar. Co.*, 309 U.S. 506, 511 (1940).

This principle of fundamental fairness extends to the Government's privileges related to classified information and the national security. Although the Classified Information Procedures Act ("CIPA"), 18 U.S.C. app. 3 §§ 1-16, provides a measure of protection to classified information in the course of prosecutions, the Government may not use its provisions to secure a material litigation advantage. The Government is required instead to abandon the claim where litigation of the claim or a related defense depends on information the Government chooses not to disclose. See *id.* § 6(e)(2) (dismissal of claim or count, or finding against Government). Similarly, outside the context of CIPA, the Government must choose between pursuing a prosecution and invoking executive privilege to protect classified information or other government secrets material to a defense against the Government's case. See *United States* v. *Smith*, 780 F.2d 1102, 1107-08 (4th Cir. 1985) (en banc); see also *Roviaro* v. *United States*, 353 U.S. 53, 60 (1957).

The court of appeals reasoned that a different result is warranted here because, it believed, the contractors "are not at jeopardy from an attack on them by the government," but rather "are the plaintiffs in this purely civil matter, suing the sovereign on the limited terms to which it has consented." App. 208a. Therefore, the "Fifth Amendment does not require that they be able to present all defenses[.]" *Id.* at 208a-209a. That ruling fundamentally misconceives the nature of the Government's claim, the unique scheme the Government has established to resolve government contract disputes, and the due process implications of stripping the contractors of their defense.

The fact that this case arises in the civil, rather than the criminal, context is not relevant, for even in civil cases, a litigant must be given an "adequate opportunity to defend against the imposition of liability." *Nelson*, 529 U.S. at 466. As previously noted, *supra* at p. 11, the effect of a termination for default is not only to deprive a contractor of profits it would have made on the contract, but also to require the contractor to repay the monies it received for services performed on the Government's behalf and perhaps to reduce or eliminate the contractor's ability to receive additional government contracts in the future. Thus, while the Government does not seek to deprive the contractors of liberty in this case, it most certainly seeks, through its default termination claim, to require them to pay billions of dollars to the Government.

The Federal Circuit's analysis thus rests on the empty formalism of labeling the contractors as "plaintiffs" and disregards the due process principles associated with when a court may grant relief to a party on its claim or compel payment by a losing

party. And, even the court's labeling is mistaken. As previously discussed, *supra* at pp. 10-12, the contractors are styled as plaintiffs in this case only because the Government gave itself (acting through the contracting officer) the power to determine when its contractors are in breach of contract, and made that determination final and legally binding unless challenged by the contractors. See 41 U.S.C. § 605 (Contract Disputes Act). That is, the defense contractors nominally are "plaintiffs" only because the Government structured the defense contracting process to relieve itself of the normal obligation of having to sue the contractors to assert its breach of contract claim. Thus, only by elevating form over substance can the Federal Circuit hold that the posture of this litigation supports permitting the Government to use the state secrets privilege to deprive the contractors of their right to present an adequate defense—that the Government itself caused the breach of contract.

The Government's reversal of the normal litigation process is consistent with due process only because it still affords the contractors an opportunity to dispute and defend against the Government's breach of contract claim by filing a lawsuit to obtain a judicial hearing. See *Lichter*, 334 U.S. at 789-92 (upholding similar scheme under the Renegotiation Act that enabled the Government to recover "excessive profits" on military goods and services during World War II unless the contractor challenged the Government's determination in the Tax Court). Nor does any consideration related to sovereign immunity require a different result. While the United States has the sovereign authority to require a contractor to initiate a lawsuit to avoid being held liable on a government contract claim, sovereign immunity cannot erase a

contractual right—and trigger judicial enforcement against a private party—once the Government has already entered the contract. The Government's claim against its contractors is hardly analogous to the claim of a third party who, like the plaintiffs in *Reynolds*, has no contractual relationship with the Government and may sue the Government in tort only because the Government has waived sovereign immunity. In the former situation, the Government is advancing its own contract claim, which in this case could require the contractors to pay the Government more than $2.8 billion in contract payments and interest, in addition to forfeiting $1.2 billion (plus interest) in unrefunded costs incurred performing the contract. In the latter situation, "the Government is not the moving party, but is a defendant only on terms to which it has consented." *Reynolds*, 345 U.S. at 12.

Although the Fifth Amendment hardly requires the Government to answer in damages for every violation of law, it does require that when the Government seeks judicial relief against a private party and proposes to extract from it billions of dollars, that party must be afforded an "adequate opportunity to defend against the imposition of liability." *Nelson*, 529 U.S. at 466; see also, *e.g.*, *Lindsey* v. *Normet*, 405 U.S. 56, 66 (1972) (due process requires that "'there be an opportunity to present every available defense'") (quoting *Am. Surety Co.* v. *Baldwin*, 287 U.S. 156, 168 (1932)). The Federal Circuit's rule denies government contractors this opportunity to defend against government contract claims when, as in this case, the Government's invocation of the state secrets privilege precludes litigation of the contractors' defense.

The Federal Circuit's rule is particularly flawed in the context of this case because the Government can terminate the contract for convenience, which is a substantial but not one-sided remedy. See, *e.g.*, Krent, *supra*, at 1565-66 (when the Government terminates a contract for convenience, it may "escape the full consequences of a breach" because the contractor may not obtain specific performance and its recovery is generally limited to costs incurred, profit on work done, and the cost of preparing the termination settlement proposal). Thus, even leaving due process principles to one side, the Government's interests can be fully protected without depriving contractors of their defenses to government claims and thereby shifting to government contractors the entire cost of protecting classified information.[10] Cf. *Winstar*, 518 U.S. at 896 (balancing the Government's "need for freedom to legislate with its obligation to honor its contracts" by refusing to give the Government relief from its contractual commitments in "instances in which the Government seeks to shift the costs of meeting its legitimate public responsibilities to private parties"). Accordingly,

[10] The Government's suggestion that contractors might "raise a superior-knowledge claim simply to induce the government to invoke the state-secrets privilege" (Pet. Opp. at 18) is wholly unfounded. When litigating against parties that already hold security clearances and have been trusted to handle extremely sensitive information, the Government would rarely need to invoke the privilege. And, in the usual case even following invocation of the privilege (as in the initial phases of this case), the parties' claims can be litigated through the courts' traditional methods of protecting classified information and proceeding based on otherwise available evidence. *See Reynolds*, 345 U.S. at 11. In addition, defense contractors are often highly dependent on the Government's continued willingness to do business with them, which creates very considerable incentives against litigating in bad faith.

simple justice—reflected both in sound government contracting policy and due process—requires that the termination for cause be converted to a termination for convenience.

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be reversed.

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v.

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Respondent.

THE BOEING CO.,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

On Writs of Certiorari to The Court Of Appeals For The Federal Circuit

BRIEF OF THE CONSTITUTION PROJECT AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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BRIEF OF THE CONSTITUTION PROJECT AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

INTEREST OF THE *AMICUS CURIAE*[1]

The Constitution Project is an independent nonprofit organization that seeks bipartisan solutions to pressing constitutional issues. The Project brings together policy experts, legal scholars, and former government officials and judges from across the political spectrum to formulate, issue, and promote recommendations for policy reform. The Project's Liberty and Security Committee works to ensure that we protect civil liberties as well as national security.

In May 2007, members of the Liberty and Security Committee issued a report entitled *Reforming the State Secrets Privilege* (May 31, 2007).[2] More recently, the Constitution Project issued a report outlining specific recommendations for the Obama Administration and Congress regarding pressing national security issues (*Liberty and Security: Recommendations for the Next Administration and Congress* (Nov. 18, 2008)), as well as a report about over-classification within the Executive Branch (*Reining In Excessive Secrecy: Recommendations*

[1] Pursuant to Rule 37.6, *amicus* affirms that no counsel for a party authored this brief in whole or in part and that no person other than *amicus* and its counsel made a monetary contribution to its preparation or submission. The docket in this case reflects the parties' blanket consent to the submission of *amicus* briefs.

[2] HTTP addresses for this and other material we cite are included in the table of authorities.

For Reform Of The Classification And Controlled Unclassified Information Systems (July 16, 2009)).

The first two of these reports examine the state secrets privilege formulated by this Court in *United States* v. *Reynolds*, 345 U.S. 1 (1953). They express concern at how the privilege has been expanded in recent years and recommend reforms to restore the independent role of the courts in evaluating privilege claims. The Government has invoked the privilege more frequently and in more kinds of cases than ever before. And the lower courts including the Federal Circuit in this case have broadened the privilege so that, rather than simply protecting particular pieces of sensitive evidence from public disclosure, it now operates to shield the Government from accountability for violations of the Constitution, laws, and treaties of the United States. The bipartisan group of professionals who have endorsed the Constitution Project's efforts believes that, as a result, a thorough reexamination of the privilege by all three branches of government is in order. This case affords an opportunity for this Court to begin that important work.

SUMMARY OF ARGUMENT

This case is the Court's first meaningful encounter with the state secrets privilege since it first created the privilege in *Reynolds* more than a half century ago. Much has changed in that time. We have learned that *Reynolds* itself was built on a false foundation the supposedly secret military evidence at issue there was in fact nothing more than evidence of the Government's negligence. And, in the absence of additional guidance from this Court, the Executive Branch and the lower courts have gradual-

ly expanded the privilege from a limited evidentiary doctrine to a powerful litigation weapon that allows the Government to eradicate entire claims and defenses. This expansion threatens the separation of powers and has pernicious consequences for the rule of law. Indeed, in recent years, both Congress and the President have begun to recognize the dangers that the privilege poses and have proposed reform. But Congress has yet to enact any corrective legislation, and the Executive's new guidance is extremely limited. Thus, far from obviating action by this Court, those efforts only underscore the pressing need for the Court to narrow the state secrets privilege and restore it to its proper sphere. The privilege is judge-made law, after all, and the Court is the institution best suited to fix these problems.

This case presents the Court with an opportunity to rethink the privilege for a new era, one in which government secrecy has increased, the privilege has become far more prominent, and the courts have more experience handling confidential materials. The Court should hold, first, that the courts must actually examine the evidence at issue *in camera* before ruling on a privilege claim. The failure to take this simple step in *Reynolds* allowed the Government to perpetrate a fraud that has haunted the privilege for over a half century. Second, the Court should make clear that the privilege does not give license to dismiss entire cases, claims, or defenses at the outset of litigation. Federal courts have various tools to let litigation proceed even where the privilege is invoked, and they must use those options if at all possible, rather than allowing privilege invocations to terminate the adjudication more-or-less automatically. At a minimum, the Court must reject the result endorsed by the Federal Circuit here, that the privi-

lege can be used to block a litigant from defending itself against a Government claim. The state secrets privilege, like other evidentiary privileges, cannot be invoked simultaneously as shield and sword.

By confining the privilege in these ways, the Court will enable the Government to protect its secrets without unduly trammeling citizens' rights to pursue their claims or improperly immunizing the Executive against meaningful judicial review.

ARGUMENT

I. The Court Should Clarify *Reynolds* And Give Guidance To The Lower Courts About How To Apply The State Secrets Privilege.

In the more than 50 years since this Court last confronted the state secrets privilege, the privilege has gone from a relatively obscure doctrine to a centerpiece of the Executive Branch's litigation strategy in an increasingly wide and important range of cases. Without additional guidance from this Court, lower courts have tended to defer to the Government's claims of privilege, threatening to tilt the scale too much in favor of secrecy at the expense of justice and judicial independence.

A. The history and evolution of the privilege illustrates the need for reform.

This Court created the modern state secrets privilege when it decided *United States* v. *Reynolds* in 1953. Although the Court tried to balance national security concerns with adherence to the rule of law, *Reynolds* was built on what by all appearances was a brazen act of deception or at the very least, a misguided and unchecked effort to avoid embarrassment. The abuse that the Court unwittingly sanc-

tioned in *Reynolds* illustrates the dangers of too much deference to the Executive. Those dangers have been compounded in more recent years by the Government's increasing willingness to assert the privilege and by the increasing unwillingness of lower courts to provide a real check on those assertions.

1. Abuse of the privilege has been a problem from the very start.

Decided at the height of the Cold War, *Reynolds* was the first case in which the Court recognized a formal evidentiary privilege based on the protection of military or state secrets. Only decades later, however, was it revealed that in fighting for the privilege in *Reynolds*, the Government was not protecting national security, but was trying to cover up its own negligence. That cover-up taints *Reynolds*'s legacy and that of the privilege it endorsed.

Reynolds involved a suit against the federal Government by the widows of three civilian engineers killed in the crash of an Air Force B-29 aircraft. The plaintiffs claimed that the crash was caused by government negligence and sought discovery of the Air Force's official accident investigation report, which they believed would corroborate that claim. The Government declined to produce the report, asserting that its disclosure would jeopardize national security. The Air Force claimed that the B-29 was on a secret mission to test classified electronic equipment. The district court was skeptical and ordered that the documents be made available for *in camera* review. When the Government refused, the district court found in favor of the plaintiffs, and the court of appeals affirmed. *Reynolds*, 345 U.S. at 3-6.

The Government pressed on, and ultimately persuaded this Court to sustain its privilege claim. The Court began by observing that "[j]udicial experience with the privilege which protects military and state secrets has been limited in this country." *Id.* at 7. The Court then described a "formula of compromise." *Id.* at 9. On the one hand, judges are the ultimate arbiters of "whether the circumstances are appropriate for the claim of privilege" and "[j]udicial control over the evidence * * * cannot be abdicated to the caprice of executive officers." *Id.* at 8-10. On the other hand, the Court was not willing to "go so far as to say that the court may automatically require a complete disclosure to the judge before the claim of privilege will be accepted in any case." *Id.* at 10. The Court suggested that "[i]t may be possible to satisfy the court, from all the circumstances of the case, that there is a reasonable danger that compulsion of the evidence will expose military matters which, in the interest of national security, should not be divulged." *Ibid.*

Applying this framework, *Reynolds* held that the Government should not have been ordered to produce the accident report. The Court concluded that the plaintiffs' need for the secret documents "was greatly minimized by an available alternative, which might have given respondents the evidence to make out their case without forcing a showdown on the claim of privilege." *Id.* at 11; see also *ibid.* ("it should be possible for respondents to adduce the essential facts as to causation without resort to material touching upon military secrets"). The Court remanded to allow the plaintiffs to try to make their case without the privileged documents. *Id.* at 12.

Notably, the Court issued its ruling without ever actually reviewing the documents that the Air Force had claimed as privileged. The Court instead took the Government at its word that the report was highly sensitive and referred to "the secret electronic equipment which was the primary concern of the mission." *Id.* at 10.

Thus it was that for more than 50 years the Government's account of the sensitivity of the accident report went unquestioned. But in 1996, the Air Force at last declassified that report and, in 2000, the daughter of one of the civilians killed in the crash discovered the document on the Internet. See *Reforming the State Secrets Privilege* at 10-11; Louis Fisher, IN THE NAME OF NATIONAL SECURITY: UNCHECKED PRESIDENTIAL POWER AND THE *REYNOLDS* CASE 166 (2006). It was immediately obvious that the report, which the Government had so steadfastly insisted contained classified intelligence information, included nothing of the sort. The report did not mention the B-29's secret mission or any secret equipment on board. *Id.* at 167–169. Instead, it revealed that the crash was the result of the Air Force's negligence just as the plaintiffs had claimed all along. See *Herring* v. *United States*, 2004 WL 2040272, at *8 (E.D. Pa. Sept. 10, 2004), aff'd, 424 F.3d 384 (3d Cir. 2005).

It is difficult to avoid the conclusion that the Government fought so hard to avoid disclosing the report and misled several courts about its contents *not* to protect national security, but simply to avoid embarrassment (and liability). But even if the impetus for secrecy in *Reynolds* was not malevolent but simply stemmed from natural bureaucratic incentives, the point is that the courts easily can and

should serve as a critical check on the Executive's penchant for secrecy. Had this Court or the lower courts actually inspected the challenged evidence, the Government's ruse would have been exposed and justice could have been done. Instead, *Reynolds*'s remarkable after-history confirms that, absent meaningful judicial oversight, the state secrets privilege offers the Executive a convenient tool for using dubious claims of national security to avoid scrutiny of its actions. The shadow of *Reynolds* haunts the privilege to this day.

2. The potential for abuse of the privilege is equally serious today.

Unfortunately, the unwarranted secrecy illustrated by *Reynolds* does not represent an isolated incident. Government secrecy is a growth business, see, *e.g.*, *Reining In Excessive Secrecy* at 1-3; Dana Priest & William Arkin, *Top Secret America: A hidden world, growing beyond control*, WASH. POST, July 19, 2010, at 1, and the opportunities for improper classification and misuse of the state secrets privilege are greater than ever.

Senior executive branch officials themselves have estimated that somewhere between 50 and 90 percent of documents classified for national security purposes should never have been so classified.[3] The

[3] See *Emerging Threats: Overclassification and Pseudo-classification: Hearing Before the Subcommittee on National Security, Emergency Threats and International Relations of the H. Committee on Government Reform*, 109th Cong. 115 (Mar. 2, 2005) at 120-121, 125 (prepared statement of Thomas Blanton, Executive Director, National Security Archive) (citing Carol Haave, Deputy Undersecretary of Defense for Counterintelligence and Security in the George W. Bush administration, for the 50% estimate, and Rodney McDaniel, executive secretary of

bureaucratic tendency to overclassify has only increased in recent years, which have seen the promulgation of secret laws[4] and even secret legal theories.[5] Classification is only increasing. According to the Information Security Oversight Office, the Government made 9 million new classification decisions in 2001, 11 million in 2002, 14 million in 2003, 15 million in 2004, 14 million in 2005, 20 million new classification decisions in 2006, and a breathtaking 54 million decisions in 2009. Declassification, on the other hand, has remained stagnant.[6]

This is perhaps not surprising. There are bureaucratic incentives to over-classification, among

the National Security Council under President Reagan, for the 90% estimate). See also *id.* at 121 ("It quickly becomes apparent to any person who has considerable experience with classified material that there is massive overclassification and that the principal concern of the classifiers is not with national security, but with governmental embarrassment of one sort or another.") (emphasis omitted) (quoting Erwin Griswold, Editorial, *Secrets Not Worth Keeping: The Courts and Classified Information*, Wash. Post, Feb. 15, 1989, at A25).

[4] Steven Aftergood, *The Secrets of Flight: Why Transportation Security Administration Guards Don't Have To Tell You What They Won't Tell You*, www.slate.com, Nov. 18, 2004, (describing fact that certain federal regulations governing airport security have been classified as "sensitive security information" and therefore may not be disclosed); see also Harold Relyea, *The Coming of Secret Law*, 5 GOV'T INFO. Q. 97 (1988).

[5] Editorial, *Injustice, in Secret*, WASH. POST, Feb. 21, 2005, at A26 (describing how the Justice Department urged dismissal of *United States* v. *Abu Ali*, 395 F. Supp. 2d 338 (E.D. Va. 2005), on the basis of a secret argument, claiming that the "legal argument itself cannot be made public without disclosing the classified information that underlies it").

[6] See INFORMATION SECURITY OVERSIGHT OFFICE, REPORT TO THE PRESIDENT 2009, at 10 (2010).

them that secrecy is a tried and true strategy to evade accountability and, sometimes, the law. See *Reining In Excessive Secrecy* at 1 ("excessive secrecy and over-classification remove vast amounts of information from public scrutiny, shielding misconduct and impeding oversight"). That appears to be reflected in the sheer volume (and increasing number) of state secrets privilege claims in recent years. By all measures, the Government's use of the privilege has increased dramatically. In a 2007 article, Professor Robert Chesney reviewed all the published cases since *Reynolds* in which the Executive invoked the state secrets privilege. Robert M. Chesney, *State Secrets and the Limits of National Security Litigation*, 75 GEO. WASH. L. REV. 1249 (2007). The numbers showed a striking uptick in the use of the privilege since the 1970s. While the privilege was asserted only twice between 1961 and 1970 and 14 times between 1971 and 1980, it was asserted 23 times between 1981 and 1990, 26 times between 1991 and 2000, and 20 times between 2001 and 2006. *Id.* at 1315; see also, *e.g.*, Amanda Frost, *The State Secrets Privilege and Separation of Powers*, 75 FORDHAM L. REV. 1931, 1939 (2007).

3. In the absence of additional guidance from this Court, lower courts have shown increasing willingness to avoid meaningful scrutiny of privilege claims.

With ever more information subject to classification and with the state secrets privilege a more important part of the Government's litigation arsenal, the need for judicial vigilance against abuse of the privilege is greater than ever. But because this Court has not revisited the privilege in any meaningful way since *Reynolds*, the lower courts have struggled with

how to apply the *Reynolds* framework in an ever-widening variety of cases, including those alleging racial discrimination,[7] retaliation against whistleblowers,[8] misconduct by the CIA,[9] and extraordinary rendition.[10] The results are unsettling.

The government's invocations of the privilege have been largely successful. Of the 89 opinions that Professor Chesney catalogued, the courts issued rulings on the merits in 78 cases. In 69 of those cases, the court sustained the privilege claim in whole or in part, and in 9 cases, it denied the claim or found the information was no longer secret (i.e., time had passed and the information was no longer classified). See Chesney, 75 Geo. Wash. L. Rev. at 1315-32.

Particularly significant is the fact that the Executive Branch has increasingly used the privilege not just to wall off certain evidence from discovery, but to try to dismiss entire cases or claims.[11] Professor Chesney found that the Executive invoked the

[7] *Sterling* v. *Tenet*, 416 F.3d 338 (4th Cir. 2005).

[8] *Edmonds* v. *U.S. Dep't of Justice*, 323 F. Supp. 2d 65, 67 (D.D.C. 2004), aff'd, 161 F. App'x 6 (D.C. Cir. 2005).

[9] *Black* v. *United States*, 62 F.3d 1115, 1118-19 (8th Cir. 1995).

[10] *Mohamed* v. *Jeppesen Dataplan, Inc.*, 614 F.3d 1070 (9th Cir. 2010) (en banc); *El-Masri* v. *United States*, 479 F.3d 296 (4th Cir. 2007);

[11] See, *e.g.*, *Sterling*, 416 F.3d at 341, 347-349; *Trulock* v. *Lee*, 66 F. App'x 472, 473 (4th Cir. 2003) (per curiam); *Black*, 62 F.3d at 1116-1117, 1120; *Bowles* v. *United States*, 950 F.2d 154, 155 (4th Cir. 1991); *In re Under Seal*, 945 F.2d 1285, 1286-1288 (4th Cir. 1991); *Zuckerbraun* v. *Gen. Dynamics Corp.*, 935 F.2d 544, 545 (2d Cir. 1991); *Weston* v. *Lockheed Missiles & Space Co.*, 881 F.2d 814, 815-816 (9th Cir. 1989); *Fitzgerald* v. *Penthouse Int'l, Ltd.*, 776 F.2d 1236, 1243 (4th Cir. 1985); *Edmonds*, 323 F. Supp. 2d at 65.

privilege to seek outright dismissal in five cases between 1971 and 1980, out of 14 cases during that period in which the Executive asserted the privilege at all (36% of invocations); 9 of 23 cases between 1981 and 1990 (39%); 13 of 26 cases between 1991 and 2000 (50%); and 15 of 20 cases between 2001 and 2006 (75%). Chesney, 75 GEO. WASH. L. REV. 1249 (App.); see also Frost, 75 FORDHAM L. REV. at 1939 ("the Bush Administration * * * has sought dismissal [based on the state secrets privilege] in ninety-two percent more cases per year than in the previous decade"). This new expansive use of the privilege continues today, and contrasts with cases in prior decades in which the privilege was applied narrowly to block only specific information requested in discovery, with the litigation otherwise being allowed to proceed.[12]

In this case, for example, the Federal Circuit applied the privilege to strip petitioners of their right to present a "superior knowledge" defense to the Government's default termination claim. As a result, petitioners were precluded from mounting a meaningful defense against a Government claim that, if successful, carried a forfeiture penalty of over $5 billion. The court of appeals expressly rejected the argument that the Executive could not affirmatively invoke the privilege to deprive a private litigant of an otherwise valid defense against a Government claim. The court

[12] See, *e.g.*, *Northrop Corp.* v. *McDonnell Douglas Corp.*, 751 F.2d 395 (D.C. Cir. 1984); *Ellsberg* v. *Mitchell*, 709 F.2d 51, 59-60 (D.C. Cir. 1983); *Halpern* v. *United States*, 258 F.2d 36, 44 (2d Cir. 1958); *Am. Tel. & Tel. Co.* v. *United States*, 4 Cl. Ct. 157, 159, 162 (Cl. Ct. 1983); *In re "Agent Orange" Prod. Liab. Litig.*, 101 F.R.D. 97, 98 (E.D.N.Y. 1984); *O'Keefe* v. *Boeing Co.*, 38 F.R.D. 329, 336 (S.D.N.Y. 1965).

thus allowed the Government to maintain its litigation claim and block any discovery of evidence that might have undermined the validity of that claim. Pet. App. 207a-210a.

Even more broadly, in two prominent recent cases challenging extraordinary rendition, courts relied on the privilege to dismiss the plaintiffs' claims before any discovery was taken. In *El-Masri* v. *United States*, 479 F.3d 296 (4th Cir. 2007), the plaintiff alleged that he was mistakenly held in U.S. custody for months while he was beaten, drugged, interrogated, and placed in solitary confinement at a CIA "black site" in Afghanistan. The Government asserted the privilege, and the Fourth Circuit upheld the dismissal of the case at the pleadings stage. It did so without even giving the plaintiff an opportunity to try to prove his case using alternative, unclassified sources of evidence. *Id.* at 313; see also, *e.g.*, Steven D. Schwinn, *The State Secrets Privilege in the Post-9/11 Era*, 30 PACE L. REV. 778 (2010).

The Ninth Circuit accepted a similarly aggressive expansion of the privilege in *Mohamed* v. *Jeppesen Dataplan, Inc.*, 614 F.3d 1070 (9th Cir. 2010) (en banc). There, a bare 6-5 majority applied the privilege to affirm dismissal of a suit at the pleadings stage alleging that private contractors knowingly participated in an illegal CIA rendition program. The en banc court rejected the panel's ruling that the privilege applies only "to prevent discovery of the evidence itself" and "cannot be invoked to prevent a litigant from persuading a jury of the truth or falsity of an allegation by reference to non-privileged evidence." *Mohamed* v. *Jeppesen Dataplan Inc.*, 563 F.3d 992, 1005 (9th Cir. 2009), rev'd 614 F.3d 1070. Whereas the panel and the en banc dissent would

have required the district court to make an independent assessment of whether the privilege should apply to the evidence and given the plaintiffs a chance to prove their case without evidence that was properly deemed privileged the en banc majority dismissed the litigation entirely. *Jeppesen*, 614 F.3d at 1093; see also *id.* at 1095 (Hawkins, J., dissenting).

All of this suggests a disturbing evolution of the state secrets privilege from a limited rule of evidence to what is often an absolute bar to litigation and from a narrow protection for truly confidential materials to a powerful thumb on the scale that the Executive is free to deploy without serious judicial oversight. These developments are not consistent with, much less compelled by, *Reynolds*, which expressly instructed the lower courts to try to find ways other than the privileged evidence for the plaintiffs to present their claims. See 345 U.S. at 11. Given its proven potential to erode accountability and deprive righteous litigants of their day in court, the Court should use this case to reevaluate the *Reynolds* framework and to confine the privilege to its appropriate sphere.

B. Improper application of the privilege undermines separation of powers.

Serious constitutional concerns are also raised by this pattern of increasingly expansive claims of state secrets privilege and increasing judicial deference to such claims. An overly broad application of the privilege undermines the role of the courts in our constitutional system and erodes the separation of powers.

"Liberty is always at stake when one or more of the branches seek to transgress the separation of powers." *Clinton* v. *City of New York*, 524 U.S. 417,

450 (1998) (Kennedy, J., concurring). As Madison explained, "the great security against a gradual concentration of the several powers in the same department consists in giving to those who administer each department the necessary constitutional means and personal motives to resist encroachments of the others." THE FEDERALIST No. 51, at 321-22 (C. Rossiter ed. 1961); see also THE FEDERALIST No. 47, at 301 ("The accumulation of all powers, legislative, executive, and judiciary, in the same hands, * * * may justly be pronounced the very definition of tyranny.").

One critical aspect of our system of divided government is that the federal courts have a responsibility to adjudicate the cases that come before them. See, *e.g.*, *Colorado River Conservation Dist.* v. *United States*, 424 U.S. 800, 817 (1976) (describing "the virtually unflagging obligation of the federal courts to exercise the jurisdiction given them"). "Article III establishes a 'judicial department' with the 'province and duty * * * to say what the law is' in particular cases and controversies." *Plaut* v. *Spendthrift Farm, Inc.*, 514 U.S. 211, 218 (1995) ((quoting *Marbury* v. *Madison*, 5 U.S. (1 Cranch) 137, 177 (1803)). The "judicial Power" conferred by Article III belongs to the courts alone; it may not be ceded to or exercised by any other branch. See *Northern Pipeline Constr. Co.* v. *Marathon Pipe Line Co.*, 458 U.S. 50, 58-59 (1982); *Morrison* v. *Olson*, 487 U.S. 654, 697 (1988) (Scalia, J., dissenting). An unduly expansive state secrets privilege subverts these constitutional values.

One problem occurs when courts rubber stamp privilege claims without undertaking their own examination of the evidence at issue. There is, to be sure, a legitimate place for the protection of secret

information. The President has constitutional authority "to classify and control access to information bearing on national security" and to withhold it "from unauthorized persons in the course of executive business." *Dep't of Navy* v. *Egan*, 484 U.S. 518, 527 (1988). But the Executive cannot simply dictate that certain evidence is categorically excluded from the judicial process. Determinations about what evidence is admissible in a given case necessarily affect the outcome of litigation, and the Judiciary thus has a constitutional duty to bring its own judgment to bear when a coordinate branch seeks to withhold evidence from a legal proceeding. It has long been held that neither the Legislature nor the Executive may "prescribe rules of decision to the Judicial Department of the government in cases pending before it." *United States* v. *Klein*, 80 U.S. 128, 146 (1872).

To discharge their duty, judges must be able to review the evidence subject to a claim of privilege and determine for themselves the merits of that claim. While the courts should give respectful consideration to the President's views, they must have the final say. For a court to declare that evidence is privileged, without any independent examination and merely on the Executive's say-so, abdicates that responsibility and improperly cedes control over this critical aspect of judicial procedure.

An even more serious separation-of-powers problem occurs when the state secrets privilege is used to secure the outright dismissal of entire claims or, as in this case, the rejection of entire defenses. Applying the privilege in that way lets the Executive dictate not just the evidence that can be used, but the more basic question whether a litigant can maintain its claims and defenses at all. That effectively gives ex-

ecutive officers the power to prescribe the outcome of individual cases an affront to Article III's guarantee of an independent judiciary, and an ironic one given the federal courts' historical role in protecting individuals against government abuse.

In short, an overly broad application of the privilege circumscribes the independence of the courts within their constitutional sphere, allowing the Executive to foreclose judicial remedies for those who have suffered legal wrongs. *Hepting* v. *AT&T Corp.*, 439 F. Supp. 2d 974, 995 (N.D. Cal. 2006) (to "defer to a blanket assertion of secrecy" would "abdicate" the court's "constitutional duty to adjudicate the disputes that come before it"). In consequence, "the privilege becomes a shield behind which the government may insulate unlawful behavior from scrutiny and redress by citizens." *Halkin* v. *Helms*, 598 F.2d 1, 13-14 (D.C. Cir. 1978) (Bazelon, J., dissenting).

C. Both Congress and the President have begun to recognize the need for reform of the state secrets privilege.

In recent years, both Congress and the Executive have begun to acknowledge that the state secrets privilege needs reform. Congress has proposed (but not yet enacted) a legislative overhaul of the procedures governing the privilege, while the Obama Administration has issued a new set of guidelines that the Executive Branch is supposed to follow before asserting the privilege. These efforts are encouraging, as they indicate the widespread recognition that the privilege has strayed from its foundations and become destabilizing to our constitutional system. But they certainly do not obviate the need for this Court to do its part to keep this judge-made doctrine confined to its proper sphere. To the contrary, these li-

mited reform efforts only underscore why the Court should use this occasion to begin refashioning the state secrets privilege for the 21st century.

1. Recent legislative efforts provide a blueprint for reforming the privilege.

In 2008 and 2009, bills to reform the state secrets privilege were introduced in both the House and Senate.[13] The bills included a number of significant procedural and substantive features that offer a model this Court might follow in adjusting the *Reynolds* framework.

The Senate bill would expressly bar use of the privilege as grounds for dismissing a case. S. 417 § 4055. It also would require courts to actually review each "specific item of evidence" for which the Government invoked the privilege to determine whether the privilege claim is valid. *Id.* § 4054(e)(1). Before the court could accept a privilege claim, it would have to find that the evidence "contains a state secret" and that there is "no possible means of effectively segregating it from other evidence." *Ibid.* If the court finds the evidence privileged, it would have to determine whether "it is possible to craft a non-privileged substitute * * * that provides a substantially equivalent opportunity to litigate the claim or defense." *Id.* § 4054(f). Where the United States is the defendant and refuses to provide a non-privileged substitute, the court would be instructed to "resolve the disputed issue of fact or law to which the evi-

[13] See State Secrets Protection Act, S. 2533, 110th Cong. (2008); State Secret Protection Act of 2008, H.R. 5607, 110th Cong. (2008); State Secrets Protection Act, S. 417, 111th Cong. (2009); State Secret Protection Act of 2009, H.R. 984, 111th Cong. (2009).

dence pertains in the non-government party's favor." *Id.* § 4054(g).

The progress of this legislation[14] signals a recognition by many in Congress that meaningful reform of the state secrets privilege is warranted in the absence of action from this Court. The *Reynolds* framework, established over a half century ago, had not been updated to account for the Executive's more aggressive invocations of the privilege or the federal courts' increased experience in dealing with classified materials (discussed in greater detail below, *infra* pp. 25-27). The legislation was intended to fill that void. Its goal was to restore a proper balance between the legitimate needs of secrecy and the rights of litigants, especially those seeking to hold the Government accountable when it engages in misconduct.[15]

While these bills present a compelling framework for reforming the privilege, they have not been enacted and their prospects are uncertain. In any event, the possibility of legislative action should not be a deterrent to meaningful reevaluation of the privilege by this Court. The state secrets privilege is judge-made law, and the Court is the institution best

[14] The Senate Judiciary Committee reported favorably on S. 2533 in 2008, and the House Judiciary Committee reported favorably on H.R. 984 in 2009.

[15] See Constitution Project Letter to Senate Judiciary Committee Urging Adoption of S. 417, the State Secrets Protection Act, Without Amendments, at 1 (June 3, 2009) ("It would restore checks and balances by restoring the role of our independent courts in evaluating state secrets claims."); see also Constitution Project Statement in Support of the State Secret Protection Act (H.R. 984) Submitted to the House Judiciary Subcommittee on the Constitution (June 4, 2009).

positioned to correct its misapplication. But the salutary principles articulated in the proposed legislation can and should guide the Court as it takes up the privilege in this case (and in future cases).

2. The recent Attorney General guidelines only confirm the need for this Court to reexamine the Reynolds *framework.*

Reflecting similar concerns that the state secrets privilege has been abused and unduly expanded, the Attorney General recently issued a new set of guidelines to regulate the Executive Branch's use of the privilege. See Memorandum from Eric Holder, Attorney Gen., to Heads of Executive Dep'ts and Agencies and Heads of Dep't Components (Sept. 23, 2009). While an important first step (and a welcome acknowledgment from the Executive of some of the problems with the privilege), these Guidelines only reinforce the need for this Court to impose similar, but legally binding, constraints and to further clarify the critical role of courts in evaluating privilege claims.

The new Guidelines address the circumstances under which the Executive will assert the state secrets privilege in litigation. They tighten the standards for privilege assertions, including requiring multiple levels of internal review before the claim may be invoked, and provide for increased public reporting of privilege claims. *Ibid.* In an effort to prevent the kind of abuse that occurred in *Reynolds*, the Guidelines expressly provide that the Department of Justice will not invoke the privilege for an improper purpose. *Id.* at 2. The Guidelines provide the following standard for when to assert the privilege:

> The Department will defend an assertion of the state secrets privilege ("privilege") in litigation when a government department or agency seeking to assert the privilege makes a sufficient showing that assertion of the privilege is necessary to protect information the unauthorized disclosure of which reasonably could be expected to cause significant harm to the national defense or foreign relations ("national security") of the United States.

Id. at 1.

While these Guidelines are a step in the right direction, they represent a very small first step. Although the Guidelines establish a standard for when the privilege will be invoked, they do not address what happens once the Government does assert the privilege. They say nothing about whether the Justice Department will consent to having courts independently review evidence that is claimed to be privileged. Nor do the Guidelines require Executive Branch officials to explain whether alternatives to the allegedly privileged material are available or require the Government to provide (unprivileged) substitute evidence. Most troubling, even under the new policy the Executive continues to assert that the privilege may be used to scuttle cases at the pleading stage, before the opposing party has a chance to prove its case using non-privileged evidence.

These are crucial issues. Judges are hard pressed to determine whether a privilege assertion is justified if they cannot actually examine the evidence at issue. But the Guidelines do nothing to ensure that the Executive Branch will facilitate that process. Similarly, the use of the privilege to foreclose entire cases or claims, with no meaningful consideration of

alternative modes of proof, is perhaps the most ominous expansion of the privilege that has occurred since *Reynolds*. The fact that the Guidelines preserve the Executive's claim that the privilege may be used to completely foreclose litigation without discovery or any independent judicial review demonstrates that they are insufficient to restore the privilege to its proper scope and role.

Finally, the Guidelines are neither legally binding nor judicially enforceable. The President or the Attorney General is free to depart from them without consequence, and a new administration could revoke them at will. Thus, while such internal self-regulation by the Executive is not insignificant, it is no substitute for clear instruction from this Court about how the privilege may appropriately be used.

In short, the Guidelines only reinforce the importance of the Court using this case to look afresh at the state secrets privilege. By reflecting on the judicial experience of the past half-century, along with the recent reforms proposed by the other branches, the Court has an opportunity to create a new framework for the privilege, one adapted to the needs of the present age. It is to the contours of this refined conception of the privilege that we now turn.

II. The Court Should Make Clear That The State Secrets Privilege Is A Narrow Evidentiary Privilege That Requires Independent Evaluation By The Courts And Leaves Room For Litigants To Pursue Their Claims Or Defenses By Alternative Means.

In refining the state secrets privilege, the Court should focus on two guiding principles. The first is independent judicial examination of the evidence at

issue. See *Reforming the State Secrets Privilege* at i-ii. *Reynolds* itself illustrates the dangers that follow from abdicating this responsibility. The Court should revisit the privilege in light of what we have learned about the Government's deception in *Reynolds* itself as well as about the bureaucratic incentives for over-classification more generally and make clear that judges must inspect the evidence claimed to be privileged before allowing the Executive to withhold it from the judicial process. Courts are fully competent to make those determinations without threatening national security, and they have a variety of procedural tools at their disposal to help them do so.

The second guiding principle is that the privilege is a narrow rule of evidence, not a justiciability doctrine or an affirmative litigation weapon to be wielded by the Government. Consequently, the result of a valid privilege invocation should not be the automatic dismissal of a litigant's claims or defenses. The courts must instead craft appropriate procedures to allow litigation to proceed whenever possible without compromising privileged information, and judges must make an independent assessment of whether there is enough non-privileged evidence for the litigation to proceed. See *Reforming the State Secrets Privilege* at 12-13. These principles are particularly powerful in a case like this, where the Executive seeks to deprive a private party of a defense against a Government claim. The Court should make clear that the privilege simply cannot be used in that way.

A. Judges should always review the evidence before ruling on a privilege claim.

It seems intuitive to say that before ruling on a state secrets privilege claim, the court should actual-

ly examine the evidence that the Government claims is privileged. And, indeed, in many state secrets privilege cases, courts do just that.[16] But the question of *in camera* inspection has been clouded by *Reynolds*'s suggestion that this procedure is not always required that in certain circumstances, judges may rule on privilege claims without even seeing the documents at issue. 345 U.S. at 10.

The time has come for the Court to revisit that aspect of *Reynolds* and make clear that judicial evaluation of the evidence is a prerequisite for a successful invocation of the state secrets privilege. "Any other rule would permit the Government to classify documents just to avoid their production even though there is need for their production and no true need for secrecy." *ACLU* v. *Brown*, 619 F.2d 1170, 1173 (7th Cir. 1980).[17] *Reynolds* itself illustrates that. As discussed above, the Court's willingness to uphold the privilege claim without conducting even a cursory examination of the allegedly privileged material allowed the Government to use the privilege to avoid embarrassment and conceal illegality, rather than to protect national security. The deception that oc-

[16] See, *e.g.*, *Linder* v. *Department of Defense*, 133 F.3d 17, 21 (D.C. Cir. 1998) ("In addition to reviewing the McNair declaration *in camera*, the district court examined the withheld documents."); *ACLU* v. *Brown*, 619 F.2d 1170, 1173 (7th Cir. 1980); *Heine* v. *Raus*, 399 F.2d 785, 788 (4th Cir. 1968).

[17] This is not to say that judges must themselves always look at each individual document; judges may, of course, rely on magistrates or sampling techniques in appropriate cases tools that are specifically authorized in the pending legislation (see, *e.g.*, S. 417 § 4054(d)(2); H.R. 984 § 6(b)), but which are in any event already well within judges' inherent powers.

curred in *Reynolds* could have been readily prevented by *in camera* review.

The promise of meaningful judicial review is the most effective way to ensure that the privilege is used appropriately, rather than as a cover for negligence or malfeasance. It provides a disincentive for the Government to assert the privilege where it is not warranted, counteracting the natural bureaucratic incentive to use secrecy as a deterrent to accountability. And, where a privilege claim is valid, putting the Government to its proof, rather than merely taking it at its word, makes the entire process more transparent and legitimate. It helps ensure litigants that the courts are respecting their interests even where the Government invokes national security, and that their right to obtain evidence in the judicial process has not been delegated to "the caprice of executive officers." *Reynolds*, 345 U.S. at 9-10.

Moreover, *Reynolds*'s suggestion that courts should sometimes accede to the Executive's privilege assertions without verifying for themselves that the evidence is actually privileged was based on a false premise. The Court was concerned that disclosure of the evidence at issue *even to a judge alone* might itself destroy the privilege and jeopardize national security. The Court evidently was worried that the federal courts lacked the resources and experience to protect classified information. *Reynolds*, 345 U.S. at 10. But these concerns have proven unfounded, and the passage of time has rendered this aspect of *Reynolds* anachronistic.

Since *Reynolds*, federal courts have frequently been called upon to assess claims regarding access to classified information under a variety of statutes, in-

cluding the Freedom of Information Act, 5 U.S.C. § 552(a)(4)(B) & (b)(1), the Foreign Intelligence Surveillance Act, 50 U.S.C. § 1805, and the Classified Information Procedures Act (CIPA), 18 U.S.C. App. 3. See also *Reforming the State Secrets Privilege* at 5. In these contexts, the courts are required to handle national security information, and *in camera* review of classified materials is a standard procedure. None of these statutes has ever been seriously questioned on grounds of institutional competence. To the contrary, this Court has rejected the suggestion that national security matters are "too subtle [or] complex for judicial evaluation." *United States.* v. *United States Dist. Ct. (Keith)*, 407 U.S. 297, 320 (1972).

These developments have provided the federal judiciary with considerable experience dealing with classified information, and the courts have developed a number of tools for conducting *in camera* review of such materials. For example, a court may impose a protective order to limit disclosure of the information[18]; limit the hearing to attorneys with appropriate security clearances[19]; or, in some cases, conduct the entire hearing ex parte.[20] In addition, special

[18] Such orders are common under CIPA. See, *e.g., United States* v. *Bin Laden*, 58 F. Supp. 2d 113, 116 (S.D.N.Y. 1999); *United States* v. *Rezaq*, 899 F. Supp. 697, 708 (D.D.C. 1995) (protective order provided "more than adequate procedural protections against public disclosure of classified information"); *United States* v. *Musa*, 833 F. Supp. 752, 758-61 (E.D. Mo. 1993);

[19] This procedure has been successfully used in some CIPA cases. See, *e.g., In re Terrorist Bombings of U.S. Embassies in East Africa*, 549 F.3d 146 (2d Cir. 2008); *United States* v. *Rezaq*, 156 F.R.D. 514 (D.D.C.1994).

[20] See, *e.g., United States* v. *Dumeisi*, 424 F.3d 566, 577 (7th Cir. 2005); *United States* v. *Gurolla*, 333 F.3d 944, 951 (9th Cir.

masters with the necessary security clearances can help courts evaluate information potentially harmful to national security.[21]

There have been no credible claims that judicial review in such cases has compromised national security or resulted in the mishandling of classified information. To the contrary, federal courts have consistently shown their competence in adjudicating cases that implicate national security. As former Judge Patricia Wald explained in testimony before Congress, courts "deal with national security information on a regular basis and can be entrusted with its evaluation on the relatively modest decisional threshold of whether its disclosure is 'reasonably likely' to pose a national security risk.'"[22] Former federal judge, FBI Director and CIA Director William Webster made a similar observation in his statement to Congress: "I can confirm that judges can and should be trusted with sensitive information and that they are fully competent to perform an independent review of executive branch assertions of the state secrets privilege."[23]

2003); *United States* v. *Yunis*, 867 F.2d 617, 620 (D.C. Cir. 1989).

[21] See, *e.g.*, *In re "Agent Orange" Prod. Liab. Litig.*, 97 F.R.D. 427, 429 (E.D.N.Y. 1983) (special master appointed to review classified documents relevant to a class action brought by Vietnam War veterans); *In re United States Dep't of Defense*, 848 F.2d 232, 234 (D.C. Cir. 1988).

[22] Examining the State Secrets Privilege: Protecting National Security While Preserving Accountability, Hearing before the S. Comm. on the Judiciary, 110th Cong. (Feb. 13, 2008) (prepared statement of Patricia Wald).

[23] *Ibid.* (prepared statement of William Webster).

In short, given what we now know about the tendency of the Executive to over-classify information and about the courts' competence to review classified information, there is no justification for any conception of the state secrets privilege that excludes *in camera* review of the evidence at issue.

B. A successful claim of privilege should not terminate a case or otherwise render claims non-justiciable.

The Court should also make clear that the state secrets privilege is a narrow rule of evidencc not a justiciability doctrine or a vehicle for scuttling a litigant's entire claim or defense.

That understanding of the privilege flows from *Reynolds* itself. *Reynolds* involved a concrete dispute over a concrete document. The Court ruled that the plaintiffs could not obtain and use that document, but in no way suggested that plaintiffs were barred from pursuing their claims using other evidence. To the contrary, the Court held that plaintiffs should have an opportunity to "adduce the essential facts * * * without resort to material touching upon military secrets" and remanded to allow them to do just that. *Reynolds*, 345 U.S. at 11. Thus, while the privilege formulated in *Reynolds* protects classified *evidence*, it does not and should not preclude litigants from pursuing their claims or defenses through other means. The *Reynolds* privilege, that is, is not an immunity doctrine or a rule about whether certain kinds of claims can be adjudicated in the first place.

By contrast, this Court has recognized that certain types of cases "lawsuits premised on alleged espionage agreements" are "altogether forbidden." *Tenet* v. *Doe*, 544 U.S. 1, 9 (2005). First formulated in

Totten v. *United States*, 92 U.S. 105 (1875), that rule is very narrow; it applies only in the "the distinct class of cases that depend upon clandestine spy relationships." *Tenet*, 544 U.S. at 10. The limit on *Totten*'s scope flows from its premise. The rule rests on the idea that prohibiting litigation over the substance of a clandestine employment relationship is an implied condition of the contract. *Id.* at 107 ("The secrecy which such contracts impose precludes any action for their enforcement."). Given *Totten*'s grounding in contract law, it does not extend to other cases where the party opposing the Government has not consented (even impliedly) to a bar on his right to pursue his claims.

Thus, in *Tenet* the Court expressly distinguished the "categorical *Totten* bar" from the "balancing of the state secrets evidentiary privilege." 544 U.S. at 10. The Court held that "the state secrets privilege and the more frequent use of *in camera* judicial proceedings simply cannot provide the absolute protection we found necessary in enunciating the *Totten* rule." *Id.* at 11. *Tenet* therefore confirms that the state secrets privilege is not to be conflated with the *Totten* bar. The two are distinct in scope and in operation. The privilege is a narrow evidentiary doctrine, not a categorical bar on certain kinds of litigation.

Nevertheless, as described above, lower courts have increasingly allowed the privilege to be used not simply to wall off particular evidence from discovery, but to block entire claims from even getting past the pleading stage. See, *e.g.*, *Jeppesen*, 614 F.3d 1070; *El-Masri*, 479 F.3d 296. In other cases, such as this one, the privilege has been used to strike entire claims and defenses that private litigants would otherwise have been able to pursue in litigation against

the Government. See Pet. App. 207a-210a; n.11, *supra.*

This expanded use of the privilege allows the Government to pull the plug on litigation even though the opposing party may be able to prove its claim or defense through alternative means. In consequence, the state secrets privilege is effectively being transformed into a broad justiciability doctrine, akin to the *Totten* bar. The Government is being allowed to use the privilege not to protect certain evidence, but to stop litigation in its tracks. This expansion of the state secrets privilege one not sanctioned by any of this Court's decisions poses serious dangers to our constitutional democracy. It lets the Executive effectively prescribe rules of decision in particular cases and thereby immunizes a wide swath of Government conduct from judicial review. The Court should make clear that this application of the privilege is impermissible.

Instead, under the proper conception of the privilege, a court's acceptance of a privilege claim after independently reviewing the evidence would be the first step in the analysis, not the last. Rather than dismissing the case outright, the court would be required whenever possible to craft appropriate procedures to allow the case to proceed without compromising the properly privileged information. In doing so, courts would not be writing on a blank slate. Since *Reynolds*, courts have developed various procedural innovations to allow litigation to proceed even when a case implicates state secrets. Using "creativity and care," these courts have employed "procedures which will protect the privilege and yet allow the merits of the controversy to be decided in

some form." *Fitzgerald* v. *Penthouse Int'l. Ltd.*, 776 F.2d 1236, 1238 n.3 (4th Cir. 1985).

One option is for the district court to order the Government to provide a non-privileged substitute for evidence covered by the privilege in situations where the court concludes that such a substitute would be feasible. That procedure has been used with considerable success under CIPA, which requires the Government to "provide the defendant with substantially the same ability to make his defense as would disclosure of the specific classified information." 18 U.S.C. App. 3 § 6(c)(l); see, *e.g.*, *United States* v. *Rezaq*, 134 F.3d 1121, 1143 (D.C. Cir. 1998). A substitute can take various forms, including a non-classified summary of the privileged information,[24] a redacted version of the evidence,[25] a statement by the Government admitting to the facts that the privileged evidence would tend to prove,[26] or any other substitute that the court deems fair to both parties. The goal of all these options is to put the opposing party in as close as possible to the same position as if it had access to the classified material.

Another procedural device for keeping the privilege confined to its proper sphere is to ensure that sensitive material is "disentangled from non-sensitive information to allow for the release of the latter." *Ellsberg* v. *Mitchell*, 709 F.2d 51, 57 (D.C. Cir. 1983). Courts have sometimes used special masters to help in the task of supervising discovery to

[24] *E.g.*, *Attorney General* v. *Irish People, Inc.*, 684 F.2d 928, 954 (D.C. Cir. 1982) (per curiam).

[25] *E.g.*, *United States* v. *Kampiles*, 609 F.2d 1233 (7th Cir. 1979); *United States* v. *Libby*, 429 F. Supp. 2d 1 (D.D.C. 2006).

[26] *E.g.*, *United States* v. *North*, 713 F. Supp. 1442 (D.D.C. 1989).

ensure that only truly privileged information is being withheld.[27] But, however the courts do it, the state secrets privilege should not automatically preclude a private litigant's right to pursue its claims and defenses on the merits. That does not mean that those litigants will necessarily prevail, but they should not be prematurely deprived of the opportunity to adjudicate merely because they cannot have access to certain evidence. For example, in long-running litigation brought by a plaintiff who alleged that CIA agents had dropped LSD into his drink while he sat in a Paris café, the Government was allowed to preserve the privilege by producing redacted documents. Although the privilege was sustained, the case proceeded through discovery, summary judgment, and trial. Ultimately, after a three-week trial, defendants prevailed on the merits. *Kronisch* v. *United States*, 150 F.3d 112 (2d Cir. 1998).

C. The privilege cannot be used to strip private litigants of their defenses against the Government's claims.

Finally, and particularly relevant here, the Court should make clear that the Government cannot use the privilege offensively, to strip a private litigant of a defense or otherwise prevent it from effectively defending against a Government claim. In this case, the Federal Circuit applied the privilege not just to limit petitioners in the evidence they could use, but to preclude them from even advancing one of their

[27] *E.g.*, *Loral Corp.* v. *McDonnell Douglas Corp.*, 558 F.2d 1130, 1132 (2d Cir. 1977) (special master used where a "large amount of material properly classified confidential and secret must be submitted to the trier of fact in the case"); *Hepting*, 439 F. Supp. 2d at 1010.

central defenses. Pet. App. 207a-210a. This is a particularly pernicious application of the privilege.

It is inconsistent with the very notion of an evidentiary privilege to allow the Government at once to deploy it to protect evidence and to preclude its litigation adversaries from defending against its claims. It is black-letter law that a party cannot make affirmative claims that rest on privileged evidence while relying on the privilege to prevent the opposing party from offering defenses to those claims. See, *e.g.*, *Tenenbaum* v. *Simonini*, 372 F.3d 776, 777 (6th Cir. 2004); *Kasza* v. *Browner*, 133 F.3d 1159, 1166 (9th Cir. 1998). It should be no different with the state secrets privilege. Where its affirmative claims implicate privileged material, the Government may protect its secrets only at the expense of its litigation position. See *Reforming the State Secrets Privilege* at 12. As the petitioners show in their briefs, any other approach further distorts the privilege and violates due process. Boeing Br. at 27; General Dynamics Br. at 27.

Simply put, the Government should not be allowed to pursue a claim when the state secrets privilege precludes its adversary from offering evidence to defend against that claim. Just as the Government cannot bring a prosecution in which it "invoke[s] its governmental privileges," *Reynolds*, 345 U.S. at 12, in a civil case like this the Government cannot assert an affirmative claim while at the same time invoking the privilege so as to undermine any meaningful defense to that claim.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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♦

GENERAL DYNAMICS CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

♦

THE BOEING COMPANY, PETITIONER

v.

UNITED STATES OF AMERICA

♦

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

♦

BRIEF OF NATIONAL DEFENSE INDUSTRIAL ASSOCIATION AS AMICUS CURIAE SUPPORTING PETITIONERS

♦

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The National Defense Industrial Association (NDIA) respectfully submits this brief as amicus curiae in support of petitioners.[1]

INTEREST OF AMICUS CURIAE

The NDIA is a non-partisan, nonprofit organization with a membership that includes over 1,700 companies and 80,000 individuals. NDIA's members provide a wide variety of goods and services to the government and include some of the Nation's largest defense and homeland security contractors. Among other things, NDIA's members perform, and may be asked in the future to perform, large-scale research and development contracts with the government similar to the one awarded to petitioners here to design, manufacture, and test the "A-12 Avenger" aircraft.

[1] Pursuant to Rule 37.3(a), blanket letters consenting to the filing of this brief by the parties have been filed with the Clerk of the Court. No counsel for a party authored this brief in whole or in part, and no party or counsel for a party made a monetary contribution intended to fund the preparation or submission of the brief. No person other than amicus curiae, its members, or its counsel made a monetary contribution to the preparation or submission of this brief.

The issue in this case raises matters of substantial interest to NDIA's members, because it affects the manner in which the government can subsequently justify in court its termination of a government contract, and in particular a billion dollar fixed-price research and development contract. The Federal Circuit's ruling permits the government to expose NDIA members to the severe consequences of default termination—due to waning political or economic support for a project—while simultaneously preventing the contractor from mounting a defense against that termination due to the government's invocation of the state-secrets privilege. Such a result severely undermines NDIA's members' abilities and incentives to bid on and undertake future government contracts.

SUMMARY OF ARGUMENT

The United States depends on private contractors to provide assistance and materials for all facets of government operations. This is particularly true with respect to national defense, where NDIA's members provide the United States with cutting-edge technology to defend the nation from enemies all over the world. The ruling below, if not reversed by this Court, significantly undermines a contractor's incentive to enter into costly research and development contracts, and, at a minimum, increases the costs that the government, and ultimately the taxpayers, must pay to acquire new defense technologies.

A. The state-secrets holding in this case will have a profound effect on government contractors, including NDIA's members. The government possesses extraordinary power to terminate its contracts. Under the Federal Acquisition Regulation, the government can simply walk away from any contract by terminating it for convenience, with virtually no consequences to the government. The government also can, as it did in this case, terminate a contract for default, which imposes severe consequences and penalties on the contractor. But in any litigation over the propriety of such a default termination, the government must prove de novo its default claim against the contractor.

By permitting the government to use the state-secrets privilege to foreclose a contractor's defense against a default termination, the Federal Circuit

shifts the balance of power too far in favor of the government and injects new uncertainty in the contracting process. Many government contracts require the contractor either to use or to develop classified information. After the ruling below, the mere existence of this top-secret information provides the government with a potential basis to invoke the privilege whenever the contractor seeks to raise a valid defense to the government's claim of default.

B. The Federal Circuit's decision will have substantial negative effects on the government-contracting industry. The Department of Defense invests hundreds of billions of dollars in government contracts and relies on those contracts to provide a wide array of services. But uncertainty and fundamental unfairness will result from the unchecked authority bestowed on the government by the Federal Circuit's decision. As such, the decision either will discourage contractors from engaging in particularly risky or difficult-to-achieve contracts with the government or will cause such engagements to become more costly to taxpayers.

More specifically, and more importantly, the Federal Circuit's decision will discourage major research and development projects. These projects are the foundation of significant advances to our Nation's defense, yet they often require flexibility as contractors are asked to work in uncharted territory. It is commonplace for these contracts to experience cost and schedule overruns. The government often waives those overruns based on its own recognition,

and its superior knowledge due to access to classified information, that the contract goal was not attainable in the time or under the terms originally contemplated. Under the ruling below, that common reality is now a basis for a default termination even where the government has waived certain contract requirements. And the government will be able to use the state-secrets privilege to insulate that termination from meaningful review in any subsequent judicial proceeding. Such a result will discourage contractors from entering into these contracts in the future.

ARGUMENT

THE FEDERAL CIRCUIT'S STATE-SECRETS RULING IS WRONG AND CONFERS VIRTUALLY UNCONSTRAINED POWER ON THE GOVERNMENT WHEN DEFENDING ITS DEFAULT TERMINATIONS OF CONTRACTS INVOLVING CLASSIFIED INFORMATION

In *United States v. Reynolds*, this Court held that the state-secrets privilege permits the United States to prevent the disclosure of information if "there is a reasonable danger that compulsion of the evidence will expose military matters which, in the interest of national security, should not be divulged." 345 U.S. 1, 10 (1953). The Court explained that the government could refuse, by invoking the state-secrets privilege, to produce certain documents sought by a private plaintiff in a Federal Tort Claims Act suit. *Id.* at 6-7.

In upholding the invocation of the state-secrets privilege, however, the Court observed that "the

Government [wa]s not the moving party" in the litigation. 345 U.S. at 12. The Court thus distinguished the situation there from the "unconscionable" circumstance where, as here, the government *pursues* a claim "and then invoke[s] its governmental privileges to deprive the accused of anything which might be material to his defense." *Ibid.* As a moving party, this Court observed, the government "can invoke its evidentiary privileges only at the price of" relinquishing its claim. *Ibid.* Thus, this Court has recognized that the government must relinquish its claim against an accused if the government withholds documents, even due to "vital national interests," that are necessary for the accused's defense. *Jencks v. United States*, 353 U.S. 657, 670-672 (1957); *see also Roviaro v. United States*, 353 U.S. 53, 60-61 (1957) (recognizing that governmental privileges "must give way" where the disclosure "is relevant and helpful to the defense of an accused").

As petitioners demonstrate, when the government has invoked the state-secrets privilege to defeat a defense to liability, permitting the government to prevail in court on its claim is inconsistent not only with *Reynolds* but with fundamental notions of Due Process. NDIA and its members do not dispute that issues of national security can, and should, require the government to restrict access to classified information. And they recognize that the government's unilateral decision to invoke the state-secrets privilege often must go unchallenged, as even in camera review of the classified information can

threaten national security. But the price for the government's invocation of this privilege should not be borne by the party against whom it is asserted. Rather, the government must forfeit its claim against the contractor. Otherwise the judicial system will be distorted, as contractors will be deprived of the ability to defend themselves against the government's claim. And, as discussed below, because the government is not subject to contract-breach damages, the price the government must pay is small.

A. Because The Government Possesses Significant Power To Terminate Contracts For Default, The Court Should Not Permit The Government To Invoke The State-Secrets Privilege Without Consequence

1. As the present case demonstrates, the government possesses extraordinary power to terminate its procurement contracts. The Federal Acquisition Regulation, which governs every federal procurement contract, allows the government to terminate a contract at any time, for almost any reason, for its own convenience. 48 C.F.R. § 49.101(a). There are virtually no consequences to the government for a termination for convenience. The government simply walks away from the deal and must only reimburse the contractor for costs reasonably incurred and (in some cases) a reasonable profit on those costs. *Maxima Corp. v. United States*, 847 F.2d 1549, 1552 (Fed. Cir. 1988).

In certain circumstances, when the contractor fails to meet its contractual obligations, the government

can terminate a contract for "default." 48 C.F.R. § 49.101(a). The consequences to the contractor of a default termination are severe. *DeVito v. United States*, 413 F.2d 1147, 1153 (Ct. Cl. 1969). The contractor is denied payment for out-of-pocket costs that have not already been reimbursed, and the contractor may be required to pay back all progress payments it has received for work that has not yet been accepted by the government. 48 C.F.R. § 49.402-2(a). A default termination also can result in the contractor being barred from public contracting, or being prejudiced in the award of new contracts. *Id.* § 9.406-2(b)(1).

After the fact, contractors can contest a default termination in court and require the government to prove de novo the grounds for default. And if the government fails to demonstrate that a default termination was justified, the termination for default will be set aside. But rather than awarding contract-breach damages to the contractor, the termination is converted into one for the government's convenience. *Darwin Constr. Co. v. United States*, 811 F.2d 593, 597 (Fed. Cir. 1987). Thus, the only downside to the government in terminating a contract for default is really no downside at all. In its worst case scenario, the government simply walks away in a termination for convenience.

2. The ruling below further stacks the deck against contractors, and it injects new uncertainty into the contracting process. This result will have significant negative implications on future defense procurement.

Many government contracts, and particularly those in the defense industry where NDIA's members have expertise, require contractors to use and develop classified technology. In many of these contracts, the mere existence of this classified information could provide the government with the basis to invoke the state-secrets privilege whenever the contractor seeks to raise a valid defense to a government claim of default. This result is aggravated by the fact that, under the ruling below, the government is permitted to articulate a post-hoc justification for its decision to terminate the contract for default. GD Pet. App. 269a; Boeing Pet. App. 95a. Thus, the government can terminate a contract due to waning political support for a program, GD Pet. App. 411a; Boeing Pet. App. 442a ("In the end, the contract was not terminated because of contract default. It was terminated because the Office of the Secretary of Defense withdrew support and funding."), and then justify the termination after the fact on grounds that are entirely unrelated to the government's motivation. Indeed, because the Federal Circuit requires only some "nexus between the government's decision to terminate for default and the contractor's performance" for a default termination to be sustained, GD Pet. App. 269a; Boeing Pet. App. 95a, the government can intentionally articulate a basis for default during the course of litigation that implicates classified information and the state-secrets privilege.

Accordingly, if left standing, the Federal Circuit's ruling will place NDIA's members in a fundamentally

untenable and unfair situation with respect to many of their contracts: if the government were to terminate those contracts on an allegation of default, the government could preclude the contractor from raising valid defenses while still subjecting the contractor to the government's forfeiture claim. This troubling result is unnecessary, as the government suffers very little prejudice if its invocation of the privilege results in a termination for convenience. That consequence is hardly the equivalent of letting a potential criminal go free, a result that is accepted when the government invokes the state-secrets privilege against someone it criminally has accused. *See, e.g.*, *Jencks*, 353 U.S. at 671-672. Indeed, here, the government's invocation of the state-secrets privilege means that it would not even have to pay all of the usual termination-for-convenience costs to the contractors. *See* Boeing Br. 17-20; GD Br. 13-14, 58-61. Moreover, where the government decides it needs to invoke its state-secrets privilege, a termination for convenience of the government is the appropriate result.

Further, because courts defer to the government when reviewing an invocation of the state-secrets privilege (lest that scrutiny result in the disclosure of the very information the privilege is designed to protect), the government's assertion of the privilege is almost never successfully contested (if it is even contested at all). *See, e.g.*, *El-Masri v. United States*, 479 F.3d 296, 305-306 (4th Cir. 2007). As this Court has explained, the propriety of the invocation often is immune even from in camera review. *Reynolds*,

345 U.S. at 10. Thus, the government has every opportunity and motive to assert the privilege, even where it might be unnecessary or inappropriate to do so.

Reynolds itself provides a potential example of just such a case. Fifty years after that decision, access to previously classified reports raise serious questions as to the legitimacy, or at least the necessity, of the government's privilege claim. *See Herring v. United States*, No. 03-cv-5500, 2004 WL 2040272 (E.D. Pa. Sept. 10, 2004), aff'd, 424 F.3d 384 (3d Cir. 2005). When it was finally disclosed, the report discussed nothing about secret military equipment on board the aircraft that crashed. Erin M. Stilp, Note, The Military & State-Secrets Privilege: The Quietly Expanding Power, 55 Cath. U. L. Rev. 831, 843-845 (2005). Instead, it discussed the military's negligence in the crash. *Ibid.*

B. The State-Secrets Privilege, As Applied Below, Will Hinder The Nation's Ability To Develop Cutting-Edge Defense Technology

1. As NDIA's members can attest, the relationship between our government and its contractors depends on principles of trust and fairness, because the government possesses unique power to terminate its contracts. Just as the government invests significant taxpayer resources into contracts with its contractors, contractors—including many of the Nation's most important businesses—invest billions of dollars of their own funds into research and development to meet contractual obligations.

The uncertainty and fundamental unfairness that result from the Federal Circuit's decision will discourage contractors from engaging in risky or difficult-to-achieve contracts with the government. At a minimum, the Federal Circuit's ruling, if left standing, will cause such engagements to become more costly to taxpayers. Businesses will be required to account for the possibility that the government might terminate a contract for default—even when the termination is motivated by politics or shifting priorities rather than by contractor fault—and then prevent meaningful litigation into the very propriety of that default termination by invoking the state-secrets privilege.

This unbridled authority granted to the government by the Federal Circuit places at risk current government contracts worth hundreds of billions of dollars. And it will deter contractors from entertaining certain high-risk contracts with the government in the future. Under the Federal Circuit's ruling, NDIA's members and other contractors risk arbitrary default terminations that can be insulated from judicial review due to the government's invocation of the state-secrets privilege.

Indeed, the risks are anything but inchoate. In this case, the government knew that petitioners could not fulfill the contract without access to prior classified information on stealth technology. GD Pet. App. 64a n.16; Boeing Pet. App. 137a n.16. Tellingly, the government received a much higher and more realistic bid from contractors who, unlike petitioners,

previously had worked on very similar classified technology. JA 45, 244-246, 1188-1190. And the government recognized, even before awarding the contract to petitioners, that petitioners lacked the knowledge to appreciate the risks of, and to perform under, this contract. But the government did not share the needed information with petitioners, either before contract award or in a timely or sufficient extent during contract performance. Meanwhile, petitioners spent hundreds of millions of dollars every month from their own coffers to perform. Now, the Federal Circuit has allowed the government to impose a multi-billion dollar forfeiture on the contractors while invoking the state-secrets privilege to deprive the contractors of this defense to that claim.

If this result is allowed to stand, an observation made by the Chief Judge of the United States Court of Federal Claims in another case will be apt. There, after recognizing that "the dollars at stake" were "so large" that they caused the government to act in an unjust way, the Chief Judge observed that "one is almost tempted to wonder if insanity is indeed a prerequisite for contracting with the Government." *California Fed. Bank v. United States*, 39 Fed. Cl. 753, 754, 767 (1997). But NDIA's members are not "insane." Thus, unless the ruling below is reversed, the outcome will influence future contracting decisions when contractors decide whether to enter into new contracts and on what terms.

2. Nor should there be any doubt as to the significance of the ruling on government procurement.

As staggering as the multi-billion dollar forfeiture here is, it represents only a small fraction of the Department of Defense's overall annual investment in government contracts.

In 2008, the Department of Defense dedicated more than $200 billion in *services* contracts alone. *See* GAO, Report No. 10-39, *Defense Acquisitions: Further Actions Needed to Address Weaknesses in DOD's Management of Professional and Management Support Contracts*, at "Highlights" (Nov. 2009). And for weapons defense programs, like those at issue in this case, the Department of Defense has planned to invest nearly $900 billion over the next 5 years – the highest level in two decades. *See* GAO, Report No. 08-467SP, *Defense Acquisitions: Assessment of Selected Weapons Programs* 1 (Mar. 2008). These staggering investments by the government undermine any argument that the ruling below can be limited to the facts of this particular case. The hundreds of billions of dollars invested in numerous contracts—many of which involve significant research and development like the contract at issue here—virtually guarantee that these issues will arise again.

Indeed, the ruling below will discourage contractors from entering new contracts, which will ultimately harm the government, as it will be unable "to obtain needed goods and services" that contractors provide. *United States v. Winstar Corp.*, 518 U.S. 839, 913 (1996) (Breyer, J., concurring). This will occur at a time when the government can ill afford any such reduction, as contracted services extend far

beyond weapons defense programs. Contractors are increasingly relied on "to perform core agency missions." GAO, Report No. 08-572T, *Defense Management: DOD Needs to Reexamine Its Extensive Reliance on Contractors and Continue to Improve Management and Oversight*, at "Highlights" (Mar. 2008). Contractors are used in various roles for a number of operations, such as those in Iraq and Afghanistan. *See* GAO, Report No. 10-492, *Warfighter Support: DOD Needs to Improve Its Planning for Using Contractors to Support Future Military Operations*, at "Highlights" (Mar. 2010). As of November 2009, there were about 218,000 contractor employees operating in Iraq and Afghanistan—a number that "at times exceed[ed] the number of military personnel in each country." *Ibid.* And the Department of Defense expects to continue this heavy reliance on contractors in the future. *Ibid.*

3. Perhaps even more significant is the *type* of contract the Federal Circuit's decision discourages. Absent reversal, the ruling below will significantly discourage contractor investment into major research and development projects, which often have formed the backbone of the Nation's cutting-edge innovation, and which often are entered to counter a military threat.

When the goal is an uncharted innovation, it is difficult to establish a clear timeline for progress or completion. It is commonplace for government contracts to take longer than originally planned and to require more funding than originally expected.

See, e.g., GAO, Report No. 09-326SP, *Defense Acquisitions: Assessments of Selected Weapon Programs* 10-11 (Mar. 2009) ("Only 28 percent of DoD's major defense acquisition programs currently estimate that they will deliver on time or ahead of schedule, while just under one-half report they will have a delay of 1 year or more in delivery of an initial operational capability"); *id.* at 6 ("For DoD's 2008 programs, * * * the average delay in delivering initial capabilities is now 22 months"); GAO, Report No. 09-648T, *Space Acquisitions: Government and Industry Partners Face Substantial Challenges in Developing New DOD Space Systems*, at "Highlights" (Apr. 2009) (noting problems that "had driven up costs and schedules"); GAO Report No. 08-467SP, *Defense Acquisitions, supra*, at 8 ("DOD has already missed fielding dates for many programs and many others are behind schedule.").

Indeed, as this case makes clear, the government, which possesses significant classified information on prior projects unavailable to the contractor, often recognizes that a contract may not be capable of being fulfilled under the original timeline or specification. G.D. Pet. App. 57a; Boeing Pet. App. 129a-130a. Thus, the government frequently waives or excuses deadlines or requirements when the contract goal is more difficult to attain than initially contemplated, because the contract sets "optimistic requirements for weapon programs that require new and unproven technologies." GAO Report No. 08-467SP, *Defense Acquisitions, supra*, at 24.

Notwithstanding this acknowledgement by the government, the government frequently cancels contracts because it has reallocated funding or other priorities. GAO Report No. 09-648T, *Space Acquisitions*, *supra*, at 1 (noting that DOD has canceled programs "that were expected to require investments of tens of billions of dollars"). Contractors understand such terminations for convenience are a matter of government prerogative, but before the ruling below they did not view such shifting priorities as a potential basis for a default termination. And they did not expect that a defense against such a default termination could be totally defeated by the government's invocation of the state-secrets privilege. Unless the ruling below is reversed, NDIA's members can ill afford to make those assumptions, and undertaking future fixed-price development contracts may be "too great a risk" in most circumstances. Ralph C. Nash, *Fixed-Price Research & Development Contracts: A Risk Too High*, 23 Nash & Cibinic Rep. ¶ 39 (Aug. 2009).

CONCLUSION

For the reasons above and in petitioners' briefs, the judgment of the Federal Circuit should be reversed.

Respectfully submitted,

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